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Working Paper No 2010/13 | May 2010

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Aaditya Mattoo and Pierre Sauvé*

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The Preferential Liberalization of Services Trade

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Abstract

This chapter takes stock of the most recent wave of PTAs with a view to informing some of the policy choices developing countries face in negotiating preferential agreements in services. The chapter first considers the economics of preferences in services and asks whether services trade differs sufficiently from trade in goods as to require different policy instruments and approaches in the context of preferential liberalization. The chapter discusses whether and how PTAs in services allow deeper forms of regulatory cooperation to occur and highlights the importance for third countries of multilateral disciplines on PTAs and the criteria suggested by economic theory to minimize adverse effects on non-members. The chapter also documents a number of lessons in rule-making and market opening arising from the practice of preferential liberalization in services trade as seen from a sample of fifty five agreements (out of the 76 PTAs featuring services provisions that have been notified to the WTO to date, see Annex 1). The chapter asks whether and how PTAs differ from the GATS and whether such differences matter in policy terms.

[1] The authors are grateful to Natasha Ward and Sacha Wunsch-Vincent for their valuable comments on and written contributions to an earlier draft of this chapter.

Key findings

- The analysis of PTAs in services trade requires an extension of conventional trade theory in two ways, both of which relate to core-distinguishing features of services: first, the manner in which trade in services occurs (i.e., the typical need for proximity between the supplier and the consumer) and, second, the form that trade protection takes in the sector (i.e., restrictions on the movement of labor and capital, and stringent domestic regulations, such as technical standards, licensing and qualification requirements).
- A common effect of many restrictive measures in services trade (given their regulatory nature) is to increase the costs of operation faced by foreign providers without necessarily generating equivalent domestic rents. There is therefore little or no cost to granting preferential access because there is little or no revenue to lose. In such circumstances, preferential liberalization will necessarily be welfare-enhancing. However, countries outside the preferential arrangement may lose.
- A country is likely to benefit from eliminating, even on a preferential basis, any excessive fixed costs of entry by removing unnecessarily burdensome qualification, licensing and local establishment requirements. The presumption that a country will benefit from such initiatives is greater if agreements are not exclusionary but rather open to all parties able to satisfy the regulatory requirements maintained within the integrating area. The greatest benefits arise if recognition agreements include all countries that have comparable regulation.
- Absent liberal rules of origin on investment that confer the full benefits of an integration scheme to third country investors the establishment of preferences may result in entry by inferior suppliers. Because the most efficient suppliers may also generate the greatest positive externalities, the downside risks of preferential liberalization may be greater - especially in crucial infrastructural services. This is particularly the case in service sectors with high location-specific sunk costs requiring the establishment of a presence close to consumers. Preferential liberalization may then exert more durable effects on the nature of competition than in the case of trade in goods. For instance, concluding an agreement that allows second-best providers to obtain a first-mover advantage may imply that a country could be stuck with such providers even if it subsequently liberalizes on an MFN basis.
- The gains from preferential agreements are likely to be significant in areas where there is scope for more fully reaping economies of scale. In principle, these gains can also be reaped through MFN liberalization, but in practice the full integration of markets may require a deeper convergence of regulatory regimes. Regulatory cooperation may be more desirable - and likely more feasible - among a subset of countries than if pursued on a global scale.
- Regional and/or international harmonization or standardization can be an important and cost-effective way of improving national standards. In such situations, the best partners for regulatory cooperation are likely to be those with the soundest regulatory frameworks. Such partners may not always be found within regional compacts.
- There are gains from regulatory cooperation but also costs. The former will dominate where national regulation can be improved and where the process of regulatory convergence or

harmonization can take place, taking into account local circumstances. The costs are likely to be smallest when foreign regulatory preferences are similar and regulatory institutions are broadly compatible.

- "South-South" PTAs covering services can be looked at as a variant of the infant-industry argument. Exposure to competition first in the more sheltered confines of a regional market may help firms prepare for global competition. Firms that have gained competitiveness at the regional level may also be less likely to resist broader-based liberalization. The risk does exist, however, that regional liberalization might create a new constellation of vested interests that could resist further market opening. The GATS offers a way out of this dilemma by allowing Member countries to pre-commit to future multilateral liberalization, signaling a time-frame over which regional preferences may be progressively eroded and/or eliminated.
- The sequence of preferential market opening in services rarely, if ever, predates preferential talks in goods trade. Countries that engage in services-related PTAs either pursue such negotiations alongside merchandise trade negotiations in a manner analogous to the WTO's "Single Undertaking" approach or pursue services talks sequentially once a PTA in goods trade has been agreed.
- In practice, PTAs tend to show broad commonality, both among each other and vis-à-vis the GATS, as regards the standard panoply of disciplines directed towards the progressive opening of services markets.
- Starting with the NAFTA in 1994, an increasing number of PTAs have in recent years sought to complement disciplines on cross-border trade in services (modes 1 and 2 of the GATS) with a more comprehensive set of parallel disciplines on investment (both investment protection and liberalization of investment in goods- and services-producing activities) and the temporary movement of business people (related to goods and services trade and investment in a generic manner).[2]
- PTAs featuring comprehensive or generic investment disciplines typically provide for a right of non-establishment (i.e. no local presence requirement as a pre-condition to supply services) as a means of encouraging cross-border trade in services. Such a provision, for which no GATS equivalent exists, might prove particularly well suited to promoting digital trade.
- PTAs covering services typically feature a liberal "rule of origin"/denial of benefits clause, i.e. extend preferential treatment to all legal persons conducting substantial business operations in a member country. In practice, the adoption of a liberal stance in this regard implies that the post-establishment treatment of what is often the most important mode of supplying services in foreign markets – investment – is non-preferential (i.e. MFN equivalent) as regards third country investors.

[2] For a fuller account of the treatment of investment and the movement of labor in PTAs, see OECD (2002d) and World Bank (2005; 2006 (GEPs).)

- PTAs covering services tend to follow two broad approaches as regards the modalities of services trade and investment liberalization. A number of PTAs tend to replicate the use, found in GATS, of a positive list or hybrid approach to market opening, whereas others pursue a negative-list approach. More than half of all PTAs featuring services provisions concluded to date proceed on the basis of a negative list approach. Such agreements are more prevalent in the Western Hemisphere, reflecting the influence of the NAFTA, as well as in agreements conducted along North-South lines (with the exception of the EU and EFTA agreements).
- While both positive and negative list approaches can in theory generate broadly equivalent outcomes in liberalization terms, as a practical matter a negative list approach can be more effective in locking in the regulatory *status quo*. As well, the process of "getting there" tends to differ, with a number of good governance-enhancing features associated with negative listing, most notably in transparency terms. Studies devoted to the practice of preferential market opening suggest that North-South PTAs based on a negative list approach tend to achieve deepest, WTO+, liberalization.
- PTAs are becoming more flexible and important variations are being introduced depending on the negotiating partners. PTAs increasingly mix positive and negative list approaches under the same agreement. Recourse to negative listing is particularly pronounced in the investment area, whereas some agreements use both approaches depending on the sector or mode of supply (e.g. positive listing for cross-border trade and negative listing for commercial presence; or negative listing for banking services and positive listing for insurance services).
- A small number of governments participating in PTAs, particularly those adopting a negative list approach to liberalization, have shown a readiness to subsequently extend regional preferences on an MFN basis under the GATS. This may reflect both a realization that preferential treatment may be harder to confer in services trade (and is indeed perhaps economically undesirable with regard to investment) and that multilateral liberalization may offer greater opportunities of securing access to the most efficient suppliers, particularly of infrastructural services likely to exert significant effects on economy-wide performance.
- The issue of preference erosion remains weakly understood in services trade, and the completion of the Doha Development Agenda should provide clear empirical indications of the extent (including in sectoral terms) to which PTA signatories are willing to extend preferential commitments on an MFN basis. Studies show that the level of liberalization achieved in many PTAs exceeds current Doha Round offers by a significant margin.
- PTAs have generally made little progress in tackling the rule-making interface between domestic regulation and trade in services. Indeed, many PTAs feature provisions in this area that are no more fleshed out and, in some instances, weaker or more narrowly drawn (i.e. focusing solely on professional services) than those arising under Article VI of the GATS (including the Article VI:4 work program). More headway has been made on creating domestic regulation disciplines at the multilateral level than at the PTA level, and a large number of PTAs today affirm the desire of signatories to incorporate by reference any future progress made under the GATS Article VI:4 negotiating mandate.

- PTAs should in principle offer greater scope for making speedier headway on matters relating to regulatory co-operation in services trade, notably in areas such as services-related standards and the recognition of licenses and professional or educational qualifications. Despite the greater initial similarities in approaches to regulation and greater cross-border contact between regulators that geographical proximity can afford, progress in the area of domestic regulation has been slow and generally disappointing even at the PTA level. Several PTAs, including South-South agreements such as Mercosul or AFAS (ASEAN) have reached trade-facilitating mutual recognition agreements, notably in selected regulated professions and highly skilled occupations.
- With a few exceptions, PTAs have made little headway in tackling the key "unfinished" rule-making items on the GATS agenda. This is most notably the case of disciplines on emergency safeguards and subsidies for services, where governments confront the same technical challenges and political sensitivities at the PTA level as they do on the multilateral front. More progress has however been made at the PTA level in opening up procurement markets for services, though such advances have tended to be made in procurement negotiations rather than in the services field.
- While there is considerable diversity in terms of additional sector coverage in PTAs for individual countries, PTAs are found to go beyond existing GATS commitments and DDA offers across *all* country groupings. The PTA-induced 'jump' in sector coverage for developing countries is much larger than for developed countries, as the latter had higher sectoral coverage levels to start with under their GATS schedules.
- As regards the sectoral patterns of liberalization, the available empirical evidence attests to significant WTO+ advances across the full range of traded services. This includes both sectors that have attracted less commitments and DDA offers under the GATS - for example audiovisual services - as well as those that have generally proven more attractive in a multilateral setting, such computer, tourism or telecom services.
- The economic importance – and hence negotiating leverage – of PTA partners can exert a significant influence on the level of services liberalization flowing from preferential agreements.
- Though notable WTO+ advances can be found in may PTAs, particularly those negotiated on a North-South basis, services-related PTAs nonetheless encounter resistance to market opening in service sectors that have proven difficult to address at the multilateral level (e.g. air and maritime transport; audio-visual services[3]; movement of service suppliers; energy services).
- A number of novel advances have been made in tackling new regulatory issues or opening up new sectors in recent preferential agreements. Market-opening advances are also notable in sectors where new (post-Uruguay Round), pro-liberalization constituencies have

[3] While such a result obtains within the great majority of PTAs, some agreements, notably the Chile-Mexico FTA, the Chile-MERCOSUL FTA and the majority of PTAs involving the United States have achieved some measure of liberalization in audio-visual services. The same applies to labor mobility. See Roy, Marchetti and Hoe Lim (2006) and Sauvé and Ward (2009).

emerged seeking to use trade agreements to secure expanded opportunities in world markets. Among these are rules governing digital trade, pro-competitive disciplines in the tourism sector, express delivery services, as well as greater advances on freeing up Mode 4 trade. A number of PTAs have also begun to tackle the issue of aid for trade in services trade, albeit through non-binding provisions. In so doing, PTAs serve as useful laboratories for novel approaches to rule-making or market opening likely to inform the development of similar provisions at the multilateral level.

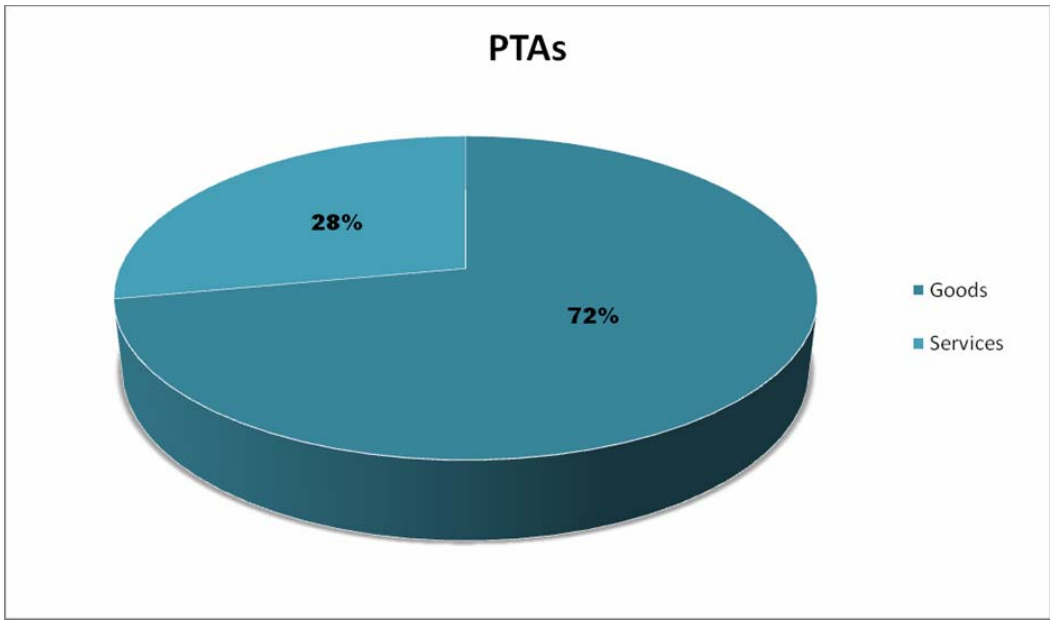
- The relationship between PTAs and the WTO is not unidirectional in character but involves iterative, two-way, interaction between the two layers of trade governance in ways that can inform, subsequent patterns of rule-making and market opening at both the PTA and WTO levels. Examples of such interaction can notably be found in areas where WTO jurisprudence has clarified or interpreted the scope of key provisions governing services trade that are typically found both in the WTO-GATS and in the services and investment chapters of PTAs.

Introduction

While there is a large literature on the costs and benefits of integration agreements on trade in goods, there is hardly any analysis of the implications of such agreements in services. Such a gap is surprising given the strong growth witnessed since the mid-1990s in the number of preferential trade agreements (PTAs) featuring detailed disciplines on trade and investment in services. The recent proliferation of PTAs covering services is evidence of heightened policy interest in the contribution of efficient service sectors to economic development and a growing appreciation of the gains likely to flow from the progressive dismantling of impediments to trade and investment in services.

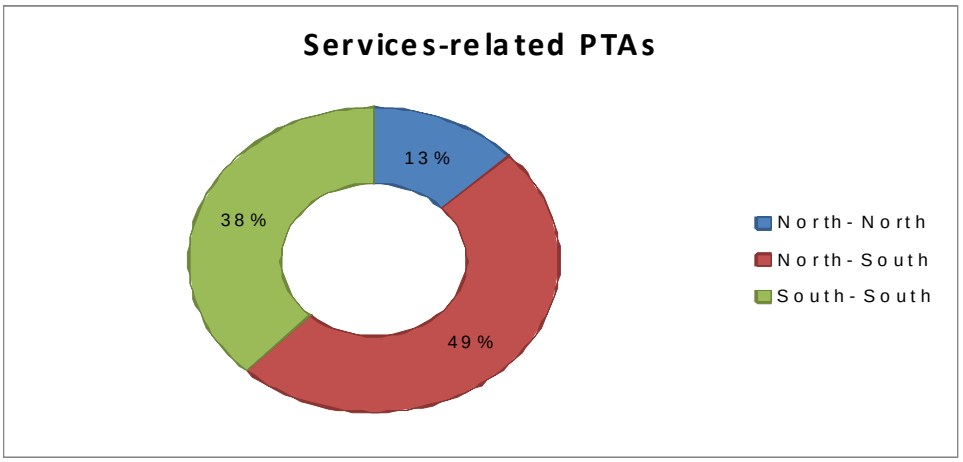
Seventy six preferential trade agreements featuring provisions on trade and investment in services have to date been notified to the WTO (See Annex Tables 1-3). This represents 28 percent of all notified PTAs, a share slightly higher than that of services in world trade (see Figure 1). Figure 2 reveals that, in line with their aggregate share in world services trade, developed countries are party to just under two-thirds (62%) of all PTAs featuring services provisions. The predominant share of such PTAs (49%) was conducted along North-South lines, with agreements among developed countries (i.e. North-North PTAs) accounting for a further 13% of notifications. Meanwhile, services-related PTAs conducted along South-South lines, while on a recent upswing, account for 38% of notified agreements. From a political economy perspective, the predominance of services-related PTAs involving developed country partners is consistent with the aggregate pattern of specialization and direction of trade and investment obtaining in services trade today.

Figure 1. Services-related PTAs as a percentage of total PTA notifications to the WTO (2010)



Source: WTO (2010).

Figure 2. Classification of services-related PTAs notified by the WTO by country groupings



Source: WTO (2010).

If all trade agreements can of essence, be likened to "incomplete contracts", then the incipient multilateral regime for services is arguably the most incomplete of all. This greatly heightens the salience of studying the relationship between preferential and multilateral regimes for services trade. This chapter takes up this challenge by considering a number of questions – both theoretical and policy-related – arising from the study of the PTA-WTO divide in services trade. Questions to which answers are sought in this chapter include the following: whether the tools of economic analysis developed for studying the effects of preference in goods trade yield meaningful insights in the services field?; to what extent, and in what form, can developments in preferential agreements inform approaches to rule-making and market opening under the GATS?; whether observed differences in negotiating architectures across services-related PTAs matter and the likelihood that such differences may inform the evolution of the WTO's post-Doha architecture of services rules?; whether the issue of preference erosion arises in services trade and what its sectoral and/or modal incidence consists of?; and whether the practice of services liberalization in services markets suggests that PTAs can be likened to "optimal regulatory convergence areas"?

Regional and bilateral attempts at developing trade rules for services continue to parallel efforts at framing similar disciplines in the WTO, under the aegis of the GATS. For this reason, regional and multilateral efforts at services rule-making are closely – indeed increasingly - intertwined processes, with much iterative learning by doing, imitation, and reverse engineering. Experience gained in developing the services provisions of PTAs has built up negotiating capacity in participating countries, providing expertise available for deployment in a multilateral setting. Since the GATS itself remains incomplete, with negotiations pending in a number of key areas (e.g., emergency safeguards, subsidies, government procurement, domestic regulation), regional and bilateral experimentations have generated a number of useful policy lessons in comparative negotiating and rule-making dynamics. As well, developments in WTO jurisprudence in the services field have begun to be reflected in patterns of market opening commitments found in PTAs, a trend that one may well expect to deepen as judicial activism under the GATS rises.[4]

The efforts that countries devote to developing rules governing the process of services-trade liberalization at the regional level typically come in the wake of the far reaching changes in many countries' services and investment policy frameworks that have taken hold in the post-Uruguay Round period. . For many countries, PTA negotiations offer the opportunity to pursue, deepen or lock in some (or much) of the policy reforms put in place domestically in recent years and to reap the benefits, notably in terms of improved investment climates, likely to flow from such policy consolidation.

[4] Evidence of such causality can be found in recent PTAs involving the United States, notably in respect of reservations made in regard to trade in on-line gambling services (Baptista Neto (2009). It may further be expected in the aftermath of the most recent WTO ruling in the dispute brought by the United States against China in the area of publications and audio-visual products (Shi and Chen, forthcoming).

This chapter takes stock of the more recent wave of PTAs with a view to informing some of the policy choices developing countries will typically confront in negotiating regional regimes for services trade and investment. While a country's choice of integration strategy will in most instances be dictated by political considerations, there remains a need for a careful assessment of the economic benefits and costs of alternative approaches to services liberalization.

The chapter focuses on two core issues. The first section considers the economics of regional integration in services, asking whether services trade differs sufficiently from trade in goods as to require different policy instruments and approaches in the context of preferential liberalization. Also discussed is whether and how PTAs may allow deeper forms of regulatory cooperation to occur. It highlights the importance for third countries of multilateral disciplines on PTAs and the criteria for PTAs not to be detrimental to non-members.

The second section addresses the political economy of regionalism in services trade, identifying a number of lessons arising from the practice of preferential liberalization in services. It does so on the basis of a sample of 55 of the 76 services-related PTAs notified to date in the WTO. Of the total, 3 of the PTAs under review relate to agreements negotiated between developed countries, 27 to agreements conducted along North-South lines and 25 to South-South agreements. .

1. The Economics of services trade in PTAs

While the economic effects of preferential tariff arrangements are generally well understood (see Chapter XX Baldwin) and form the core of conventional trade theory, such is hardly the case of services. The analysis of preferential agreements in services trade requires an extension of conventional trade theory in two ways, both of which relate to core distinguishing features of services: first, the manner in which trade in services occurs and, second, the form that trade protection takes in the sector.

Since services trade often requires proximity between the supplier and the consumer, one needs to consider preferences extended not just to cross-border trade, but also to foreign direct investment (FDI) and foreign individual service providers. Moreover, preferential treatment in services is granted not through tariffs but through discriminatory restrictions on the movement of labor and capital (e.g., in terms of the quantity or share of foreign ownership), and a variety of domestic regulations, such as technical standards, licensing and qualification requirements.

Given such differences, can one say that trade in services differs enough from trade in goods so as to modify the conclusions reached so far as regards the economic effects of preferential liberalization? In particular, what would happen if a country liberalized services trade faster in a regional or bilateral context than at the multilateral level? To answer such questions, the rest of this section will (1) review the various costs and benefits of trade preferences arising in services trade; and (2) discuss the scope for regional or bilateral regulatory cooperation in services trade.

1.1 Costs and benefits of preferential treatment in services trade

The manner in which privileged access can be granted in services markets depends on the instrument of protection in use. By imposing a quantitative restriction on services output or on the number of service providers, a country can allocate a larger proportion of the quota to a preferred source. Examples of the former abound in air, land and maritime transport, where countries often allocate freight and passenger quotas on a preferential basis, and in audiovisual services, where preferential quotas exist on airtime allocated to foreign broadcasts. Examples of the latter include restrictions on the number of telecommunications operators, banks or professionals that may be allowed to operate.

Another common means of restricting access to service markets that lends itself to preferential treatment concerns limitations on foreign ownership, on the type of allowed legal entity or on branching rights. While most host country governments provide foreign investors with post-establishment national treatment, such treatment rarely applies in the pre-establishment phase. This allows host countries to impose a range of performance requirements on foreign services providers, for instance in terms of training or employment in managerial level positions. These can easily be waived for members of a preferential arrangement.

Preferences can also be granted through taxes and subsidies. Foreign providers can be subject to different taxes and may be denied access to certain subsidy programs. Again, these forms of discrimination can be waived selectively, as is the case, for example, in co-production agreements in audiovisual services.

Another much practiced form of preferential treatment occurs through domestic regulations pertaining to technical regulations, licensing and qualification requirements. Countries can and do impose qualification and licensing requirements on foreign providers that may be more burdensome than necessary to satisfy otherwise legitimate public policy objectives. Where these are waived selectively in favor of members of a PTA, and denied to others who would otherwise qualify for the benefits, de facto preferences result. While regulatory preferences may arise in all sectors, they are especially prevalent in professional and financial services, where domestic regulatory requirements and licensing regimes respond to information asymmetries.

Measures affecting variable costs

A common effect of many restrictive measures in services trade is to increase the variable costs of operation faced by foreign providers without necessarily generating equivalent rents. In such cases, the analysis of discriminatory regulation can proceed in a manner analogous to tariffs. When tariffs are the instruments of protection, the costs of trade diversion can be an important disincentive to concluding preferential

liberalization agreements. Despite the increase in consumer surplus from any liberalization, there may still be an aversion to such agreements because the displacement of high tariff imports from third countries by low or zero-tariff imports from preferential sources implies lost revenue.

The situation may differ when the protectionist instrument is a regulatory barrier that imposes a cost on the exporter without necessarily yielding a corresponding revenue for the government or any other domestic entity. Under such circumstances, which characterize much of services trade (given the regulatory nature of impediments), there may be little or no cost to granting preferential access because there is little or no revenue to lose. In such circumstances, preferential liberalization will necessarily be welfare-enhancing.

However, countries outside the preferential arrangement may lose. Exemption from a needlessly burdensome regulation implies reduced costs for a class of suppliers and hence a decline in prices in the importing countries. This decline in prices may hurt third-country suppliers who may suffer reduced sales and a decline in producer surplus.

The analysis of discriminatory regulation is also relevant to quantitative restrictions on the sale of services. In the case of goods, the quota rents can be appropriated by domestic intermediaries like the importer rather than the foreign exporter. However, in many services, intermediation is difficult because the service is not always storable and directly supplied by producers to consumers. Rents are, therefore, usually appropriated by exporters rather than domestic importers. As in the case of frictional measures that increase variable costs, there is typically no cost of trade diversion to the preference-granting country.

The main policy implication one can draw from the above discussion is that where a country maintains regulations that impose a cost on foreign providers, without generating any benefit (such as improved quality) or revenue for the government or other domestic entities, welfare would necessarily be enhanced by preferential liberalization. However, it bears noting that non-preferential liberalization would yield an even greater increase in welfare, both nationally and globally, because the service would then be supplied by the most efficient providers.

Measures affecting fixed costs

A number of measures that countries maintain can have the effect of increasing the fixed costs of entry or establishment in services markets. Examples include requirements to establish a local presence, license fees for entry into the market, or the need to re-qualify for purposes of providing professional services. As with measures affecting variable costs, a country is likely to benefit from eliminating, even on a preferential basis, any excessive fixed costs of entry by removing unnecessary

burdensome qualification, licensing and local establishment requirements in professional and financial services.
Regardless of the chosen partners, the presumption that a country will benefit from such initiatives is greater if agreements are not exclusionary but rather open to all parties able to satisfy the regulatory requirements maintained within the integrating area. The greatest benefits arise if recognition agreements include all countries that have comparable regulation. The benefits in such instances come from both increased competition and greater diversity of services.

Measures restricting the number of service providers

The norm in many service industries is for the quantum (level) of competition to be restricted by government regulation. There may be legitimate reasons to do so, such as the existence of significant economies of scale or in industry segments characterized by natural monopoly features (the case of a number of network-based industries in energy, water distribution or transportation/railways). In such circumstances, the question of the manner in which entry is allowed - by mergers and acquisitions or through greenfield (i.e., *de novo*) investments, can assume considerable significance.
Interestingly, allowing limited new entry by foreign firms, irrespective of whether this is done preferentially or on a most-favored-nation (MFN) treatment basis, may not be welfare-enhancing. The main reason is that even though consumers may benefit from the increased level of competition, such a gain may be offset by the transfer of rents from domestic to foreign oligopolists.
Restrictions on de novo entry are often imposed with a view to channeling new foreign capital into weak or undercapitalized domestic institutions (a common occurrence in financial services for example) to help the restructuring process in the context of progressive liberalization. The above considerations may affect the preferred mode of entry: entry, that is, through acquisition implies less competition than greenfield entry, but it allows domestic firms to extract some rents through the disposal of their assets.
Liberalization tends to generate gains when all barriers to entry are removed. But if only limited entry is allowed, then open, non-discriminatory access - for instance through the global auctioning of licenses - would predominate preferential access, which cannot guarantee that preferential (i.e., insider) investors will be the most efficient ones. Absent liberal rules of origin on investment, the establishment of preferences may indeed result in entry by inferior suppliers. Because the most efficient suppliers (in terms of costs and/or quality) may also generate the greatest positive externalities (including the dynamic learning properties associated with knowledge flows and the associated rise of total factor productivity), the downside risks of preferential liberalization may be greater (Matto and Fink, 2002). The ability of non-preferential liberalization to more readily secure access to the most efficient suppliers of services is

a matter of some importance given the crucial infrastructural role many services perform and the strong influence such intermediate inputs can exert on economy-wide performance.
Preferential liberalization of entry barriers may also bring higher prices for consumers, lower takeover prices for domestic assets or lower license fees for the government (by limiting the pool of potential buyers). These concerns are likely to be compounded in concentrated markets, a common occurrence in many service industries in the developing world.

Sunk costs and the sequence of liberalization

Sunk costs are important in goods and services industries alike. However, location-specific sunk costs - those incurred in supplying a particular market - are arguably higher in a number of service sectors to the extent that their provision requires proximity between suppliers and consumers. One consequence (which is closely related to the above discussion on barriers to new entrants) is that preferential liberalization may exert more durable effects on the nature of competition than in the case of goods. For instance, concluding an agreement that allows inferior providers to establish may mean that a country could be stuck with such providers even if it subsequently liberalizes on an MFN basis.
Sunk costs matter because they have commitment value and can be used strategically by first movers to deter new entrants (Tirole, 1998). A firm that establishes a telecommunications or transport network signals that it will be around tomorrow if it cannot easily dispose of its assets. The commitment value is stronger the more slowly capital depreciates and the more firm-specific it is.
Firms allowed early entry into such types of markets may accumulate a quantity of capital sufficient to limit the entry of new rivals. Such incumbency effects may be stronger in services with network externalities, such as telecommunications, where new entrants must match the technical standards of the incumbent (standards that the latter may have also played a large part in defining). The incumbent may also succeed in assuring itself of the services of the best franchisees by selecting them early on and imposing exclusivity arrangements on them. Each of these forms of capital accumulation enhances first-mover advantages and allows the established firm(s) to prevent, restrict or retard competition.
Because of the importance of sunk costs in many service industries, sequential entry (which preferential liberalization with restrictive rules of origin may entail) can produce very different results from simultaneous entry. If entry is costly, an incumbent may be able to completely deter entry, leading to greater market concentration. Furthermore, the first-mover advantage may be conferred on an inferior supplier. The latter may naturally use such advantages to establish a position of market dominance, insulated

from more efficient third-country competitors. How durable such a position may be in practice will depend on the importance of sunk costs relative to differences in price and quality.
Two important qualifications to the above reasoning can nonetheless be made. First, subsequent entry by a more efficient firm can take place through the acquisition route, thus circumventing some of the problems linked to first-mover advantages. This has notably been the experience of a number of countries in the financial sector, especially those where first movers may have overbid or sunk excessive costs in setting up their operations in the early stages of liberalization. Second, in certain service sectors, firms could learn by doing: the experience acquired by established operators during a previous period may reduce their current costs, enhancing their profitability and discouraging others from entering. Caveats aside, a country needs to carefully evaluate not just the static costs of granting preferential access to a particular partner country, but also how the eventual benefits from multilateral liberalization are likely to be affected.

Static and dynamic economies of scale

Combining of services markets through a regional integration agreement can lead to gains arising from a combination of scale effects and changes in the intensity of competition. In a market of a given size, there is a trade-off between scale economies and competition: if firms are larger, there are fewer of them and the market is less competitive. Enlarging the market shifts this trade-off, as it becomes possible to have both larger firms and more competition (World Bank, 2000).
Regional liberalization can also act as an inducement to FDI. Apart from changing the organization of local industry, if PTAs create large markets and do not impose stringent ownership-related rules of origin, they may also assist in attracting foreign investment when economies of scale matter. For example, a foreign transport service provider might not find it worthwhile to establish in Latin America if each country market were segmented, but might find Latin America attractive with a continent-wide integrated market.
One rationale for PTAs covering services is a variant of dynamic economies of scale or the infant-industry argument. “South-South” PTAs, in particular, are seen as a form of gradual liberalization. Exposure to competition first in the more sheltered confines of a regional market may help firms prepare for global competition. This approach improves on traditional infant-industry protection because some degree of international competition is fostered as a result of the integration process. There is also the possibility that firms that have gained competitiveness at the regional level are less

likely to resist broader-based liberalization. They may even champion subsequent MFN liberalization as they begin to reap the benefits of open markets and run up against the constraints of a regional market. In this sense, as noted in Chapter XX (Baldwin & Freund), PTAs can be seen as "building blocks" towards multilateral liberalization (Bhagwati, 1990; Lawrence, 1991). The risk does exist, however, that regional liberalization might create a new constellation of vested interests that could resist further market opening, raising the concern that regionalism can become a "stumbling block" to further multilateral liberalization. The GATS offers a way out of this dilemma by allowing Member countries to pre-commit to future multilateral liberalization, signaling a time frame over which regional preferences may be progressively eroded and/or eliminated.

1.2 Regionalism and Regulatory Cooperation

The gains from PTAs are likely to be significant in areas where there is scope for reaping economies of scale, as in certain international transport and financial services, and for securing increased competition, as in business or professional services. In principle, these gains can also be reaped through MFN liberalization, but in practice the integration of markets often requires a convergence of regulatory regimes. Such convergence might well be more feasible in a bilateral or regional context, for instance when "proximity" (be it geographic or in terms of income levels or legal traditions) implies closer institutional and regulatory ties. The regulatory intensity of services trade make it necessary to consider whether and how PTAs can be conduits for trade- and investment-facilitating convergence in domestic regulatory practices. Simply put, under what circumstances is a country more likely to benefit from cooperation in a plurilateral or regional forum than in a multilateral one?

Addressing the regulatory intensity of services trade

The economic case for regulation in services arises essentially from market failure attributable to three kinds of problems: (1) asymmetric information (especially in knowledge-intensive industries, such as financial or professional services); (2) externalities (tourism, transport, water distribution); and (3) natural monopoly/oligopolies (especially in network-based services where access to essential facilities is a critical ingredient).

In the first two cases, national remedies can themselves become impediments to trade if domestic regulatory requirements are needlessly burdensome or framed with a view to tilt competitive conditions in favor of domestic suppliers. The institution of some variant of a necessity test in services agreements (the purpose of which, as in goods trade, is to ensure some broad measure of proportionality between regulatory

objectives and the means of pursuing them), together with strengthened disciplines on transparency, would enable exporters to challenge the appropriateness of regulatory regimes abroad. Doing so would help ensure that domestic regulations serve legitimate objectives rather than mask protectionist interests, and hence create benefits for domestic consumers and users of services.

In the third case (natural monopoly/oligopoly), it is the absence of regulation (typically pro-competitive regulation) that can lead to trade problems and directly inhibit and or nullify negotiated market access. As negotiations in basic telecommunications services have shown already, international rules on access to essential facilities and on means of ensuring that dominant suppliers do not abuse their market advantages to deter entry and stifle competition, can provide significant benefits to consumers and users of telecommunications services.

In order to ensure that domestic regulations at home and abroad support trade, a country must decide on the appropriate level of coordination (i.e., multilateral, regional, or bilateral), the appropriate mechanism (i.e., international rules or standards), and the appropriate approach (i.e., mutual recognition or harmonization) to pursue in individual service sectors. International rules can do little to address impediments to trade arising from fundamental differences across countries in regulatory standards. In such circumstances, two approaches can be envisaged: harmonization and mutual recognition. Even though these approaches are often presented as alternatives, the former tends to be either a precondition or a result of the latter. Where differences in mandatory quality standards matter, mutual recognition may be feasible only when there is a certain degree of prior harmonization of mutually acceptable minimum standards. A similar logic applies to compatibility standards, though there may be no alternative to full harmonization if differences matter, as for instance in the case of road-safety standards, railway gauges or legal procedures.

Regulatory cooperation may be more desirable - and likely more feasible - among a subset of countries than if pursued on a global scale. However, there is little, if any, empirical guidance on the payoffs to regulatory cooperation. What are the costs and benefits of deeper harmonization of regulatory standards and/or the establishment of mutual recognition agreements? The lack of empirical evidence complicates the task of deciding on the scope and depth, as well as the geographical reach and the optimal institutional forms, of regulatory cooperation.

If national standards are not optimal or insufficiently developed, then regional and/or international harmonization or standardization can be a way of improving such standards, as has happened in the financial services field with the Basle accord on capital adequacy. In such situations, the best partners for regulatory cooperation are likely to be those with the soundest regulatory frameworks. Such partners may not always be found within regional compacts. Moreover, the standard-setting process can at times be captured by protectionist interests, in which case convergence around “best” regulatory practice can serve a useful liberalizing purpose.

Another consideration is that there are gains from regulatory cooperation but also costs. The former will dominate where national regulation can be improved. The aggregate adjustment cost of regulatory convergence depends on the level of differences between the policy-related standards of the countries involved in an integration area. The costs are likely to be smallest when foreign regulatory preferences are similar and regulatory institutions are broadly compatible. The benefits of eliminating policy differences through harmonization depend on the prospects of creating a truly integrated market, which depends on the "natural distance" between countries, and that in turn depends on factors such as levels of development, physical distance, legal systems, and language.

If national standards optimally serve national objectives, there is a trade-off between the gains from integrated markets and the costs of transition and of departing from optimal domestic standards. For instance, a poor country may prefer to maintain a low mandatory standard for certain services because that reflects the socially optimal trade-off between price, quality and implementation capacities whereas the socially optimal trade-off in a rich country may lead to the adoption of - and a preference for - a higher standard. Under such circumstances, a harmonization of standards could create benefits in terms of increased competition in integrated markets, but would necessarily impose a social cost in at least one country. This matter may be non-trivial in the growing number of integration agreements concluded along "North-South" lines (see Box 1).

Box 1. WTO+ and WTO-X Provisions in US and EC PTAs

Horn, Mavroidis and Sapir (2009) compared substantive differences found in the PTAs of the United States (US) and the European Communities (EC). Such work drew useful attention to the distinction between so-called "WTO+" provisions, which relate to PTA-induced outcomes that build on existing WTO disciplines, and "WTO-X" provisions, which involve disciplines that have not been (or yet to be) agreed at the WTO level. The authors further draw attention to the issue of "legal inflation" in distinguishing those provisions that are legally binding and enforceable from those that are merely hortatory in nature.

Both EC and US preferential trade agreements contain a significant number of WTO+ and WTO-X obligations. However, EC agreements go much further in terms of WTO-X coverage than US agreements. When discounting for 'legal inflation' (i.e. when new provisions are not legally binding and enforceable), the picture remains largely the same for US agreements, but it changes dramatically for EC agreements.

Indeed, adjusting for 'legal inflation', US agreements typically contain more legally binding provisions, both in WTO+ and WTO-X areas, than EC agreements. Horn, Mavroidis and Sapir conclude that the EU and the US have chosen markedly different strategies for including provisions in their PTAs that go beyond the WTO agreements. In

particular, EC agreements display a fair deal of 'legal inflation', a phenomenon almost totally absent in US agreements.

While the work by Horn, Mavroidis and Sapir does not allow the authors to draw precise conclusions about this asymmetry of behaviour between the EU and the US, the fact that much of the 'legal inflation' occurs in development-related provisions, which are unique to the EC agreements, suggests that the EU has a greater need than the US to portray its PTAs as not driven solely by commercial interests. The authors speculate that such a pattern may reflect a lack of consensus on the part of EU member states about the ultimate purpose of these PTAs, such that the wide variety of provisions of weak legal value representing a compromise between various interests among EU members.

Moreover, although EC and US preferential trade agreements do go significantly beyond the WTO agreements, the number of legally enforceable WTO-X provisions contained in EC and US PTAs is still in fact quite small. Provisions that can be regarded as really breaking new ground compared to existing WTO agreements are few and far between: environment and labour standards for US agreements, and competition policy for EC agreements. All such provisions can be seen as dealing with regulatory matters. Other enforceable WTO-X provisions found in both EC and US PTAs concern domains that are closely related to existing WTO disciplines, such as on investment matters (GATS, TRIMs), capital movement (GATS) and intellectual property TRIPs).

The fact that the new, legally enforceable, WTO-X provisions all deal with regulatory issues suggests that EC and US agreements can be looked upon as vehicles of "regulatory projectionism", i.e. means for the two trade powers to export their own regulatory approaches to their PTA partners. The costs and benefits of assuming such regulatory obligations on the part of developing country partners require closer analytical scrutiny.

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PTAs as optimum regulatory areas for services

"Optimum regulatory areas" can be taught of as defining the set of countries for which aggregate welfare would be maximized by regulatory convergence. Such an area would balance the benefits and costs of participation. The benefits of eliminating policy differences through harmonization depend on the prospects of creating truly integrated markets, which depends on natural ties between countries and factors such as geographic and linguistic proximity. The costs depend on the ex ante similarity of regulatory preferences and compatibility of regulatory institutions.

In the definition of an optimal regulatory area, it must also be recognized that cooperation can be a vehicle to exchange information on different experiences with regulatory reform and to identify good regulatory practices. This form of cooperation can be especially useful for regulating new services in sectors characterized by continuous technical change. Developing countries may have a particular interest in cooperating with advanced industrial countries that have the longest experience with regulatory reform and where the newest technologies and their regulatory implications are often first introduced.

However, whether an individual country benefits from regulatory convergence or harmonization, its willingness to participate in such an area may depend on where the standard is set, the level at which it is set, and the regulatory environment to which such a standard responds. The latter factors will in turn determine who will bear the costs of transition towards the adoption of such a standard. The incentive to make regulations converge may depend on the relative size of markets, with small countries often having more to gain. This may explain why small countries acceding to the European Union (EU) accept to bear the full cost of transition.

It should be noted that the process of regulatory convergence can itself involve sunk costs of transition. The sequence in which a country chooses to harmonize (or progressively converge) its regulations with different trading partners is thus a relevant consideration. One reason is that the sequence of harmonization may influence the bargaining power of different country groupings in the negotiation over the level at which the harmonized standard should be set. For example, the countries in Eastern Europe that acceded to the EU on an individual basis could arguably have had a greater say in the EU-wide standard in specific areas if they had either been original members, negotiated collectively, or both. Similarly, harmonization first conducted at the MERCOSUR level, and then at the Free Trade Area of the Americas (FTAA) or WTO level, could imply different costs and produce a different outcome from direct harmonization at the broader level.

A final consideration to note in regard to preferential regulatory convergence relates to the possible administrative burden implied by the maintenance - and administration- of distinct regulatory requirements and procedures as between members and non-members of a PTA. Such costs may be sufficiently acute for a number of developing countries as to tilt negotiating incentives in favor of multilateral undertakings. It may also encourage the multilateralization of norms first brokered at the regional level or incite countries to simply extend to all third countries treatment similar to that afforded to PTA members, bearing in mind the limits of MFN-based outcomes on regulatory issues.

1.3 Third-Country Effects

PTAs between countries that are WTO members or accessing the WTO can be potentially harmful to non-member countries as they imply preferential liberalization in favor of certain member states. Such discrimination violates one of the central obligations imposed by both the GATT and the GATS - the MFN treatment rule. The GATS is similar to the GATT in permitting signatories to pursue preferential liberalization arrangements, subject however to a number of conditions that are intended to minimize potential adverse effects on non-members as well as on the multilateral trading system as a whole.

In the context of agreements liberalizing trade in goods, a sufficient condition for preferential liberalization to be deemed multilaterally acceptable is that it not have detrimental impacts on third countries. That is, the volume of imports by member countries from the rest of the world should not decline on a product-by-product basis after the implementation of the agreement (Kemp and Wan, 1976; McMillan, 1993). While in principle a simple enough criterion, it is not straightforward to implement in practice given that the focus is on trade flows at the individual product level.

The liberalization of services trade implies not only that measures restricting the ability of foreign suppliers to engage in cross-border trade are reduced or eliminated, but also that factor mobility (and especially the establishment of a commercial presence) is allowed.

In determining the welfare implications for third parties of regional integration agreements covering services, account therefore needs to be taken of the impact on trade *and* factor flows. Both of these flows are endogenous and interdependent. Simple prescriptions or criteria along Kemp-Wan lines therefore can no longer be applied (see Chapter XX Baldwin). If, for example, trade and factor flows are substitutes, a decline in trade in products need not necessarily be detrimental to an outside country, as greater factor flows substitute for trade. This is the standard case in neoclassical trade theory assuming constant-returns-to-scale technology. If, conversely, there are increasing returns, the relationship between factor movements and product-trade flows may well be complementary, i.e., an increase in one may be associated with an increase in the other. Although the presumption is that by liberalizing both product and factor markets, the aggregate benefits for participants will increase, and this in turn will be beneficial to the rest of the world as a whole (partly through induced growth and investment effects), straightforward criteria with which to evaluate such integration effects *ex ante* do not exist. These problems are compounded by the difficulty of establishing clear-cut criteria of product likeness in services, given the far greater degree of product differentiation and customer tailoring arising in services markets.

2. The Practice of Services Liberalization in PTAs

The previous section suggests that – in theory – the inclusion of services trade in PTAs can help achieve greater transparency through rules that require mutual openness, heightened credibility of policy through legally binding commitments, and more efficient protection and regulation through rules that favor the choice of superior policy instruments. Yet, still today relatively little is known about the actual practice of service liberalization in PTAs. What can be learnt from the experience with PTAs governing services trade? Does the bilateral or regional route to services trade and investment liberalization actually offer significant prospects for speedier and/or deeper liberalization and more comprehensive rule-making than under a multilateral framework?
This section discusses the manner in – and degree to - which PTAs covering services have indeed achieved the above mentioned theoretical objectives. It compares substantive provisions and negotiated outcomes under the GATS with progress made under a broad sample of PTAs featuring disciplines on trade in services.

2.1. Key disciplines: convergence and divergence

While PTAs covering services come in many different shapes and sizes, they tend to feature a common set of key disciplines governing trade and investment in services that are also found in the GATS, albeit with differing burdens of obligation (Table 1). Areas of greatest rule-making convergence between the multilateral and PTA levels relate to the agreements' scope of coverage. Most common to both sets of agreements, and typically drafted in an identical manner are disciplines on transparency, national treatment, MFN treatment, as well as disciplines on payments and transfers, monopolies and exclusive service providers, as well as general exceptions. Considerable similarities also exist between the multilateral and PTA levels as regards the need for sectoral specificity (i.e. individual sectors or horizontal issues (e.g. labor mobility) requiring special treatment in annexes).

Table 1: Key disciplines in PTAs covering services

Agreements	MFN Treatment	National Treatment	Market access (N-D QRs)+	Domestic Regulation	Emergency Safeguards	Subsidy Disciplines	Government procurement	Rule of origin (denial of benefits)
GATS (1994)	Yes	Yes	Yes	Yes	Future	Future negotiations	Future negotiations	Yes
NAFTA (1992)	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
Canada – Chile (1996)	Yes	Yes	Yes	Yes*	No	No	No	Yes
Canada – Colombia (2008)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
Canada – Peru (2008)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
Chile – México (1998)	Yes	Yes	Yes	Yes*	No	No	No	Yes
Bolivia-México (1994)	Yes	Yes	Yes	Yes*	Future	No	Separate chapter	Yes
Costa Rica – México (1994)	Yes	Yes	Yes	Yes*	Future	No	Separate chapter	Yes
México – Nicaragua (1997)	Yes	Yes	Yes	Yes*	No	No	Future negotiations	Yes
Mexico – Northern Triangle[1] (2000)	Yes	Yes	Yes	Yes*	Future	No	No	Yes
Central America – Dominican Republic (1998)	Yes	Yes	Yes	Yes*	Future	Future negotiations	Separate chapter	Yes
Central America –	Yes	Yes	Yes	Yes	No	No	Separate	Yes

Agreements	MFN Treatment	National Treatment	Market access (N-D QRs)+	Domestic Regulation	Emergency Safeguards	Subsidy Disciplines	Government procurement	Rule of origin (denial of benefits)
Dominican Republic – US (2004)							chapter	
Central America - Chile (1999)	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
Chile – Colombia (2006)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
El Salvador –Taiwan (2007)	Yes	Yes	Yes	Yes	No	No	No	Yes
Guatemala – Taiwan (2005)	Yes	Yes	Yes	Yes	No	No	No	Yes
Group of Three (1994)	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
MERCOSUR (1997)	Yes	Yes	Yes	Yes	No	Future negotiations	Future negotiations	Yes
Andean Community	Yes	Yes	Yes	Yes*	No	No	No	Yes
CARICOM (2001)	Not specified	Yes	Not specified	Yes*	Yes	No	No	Yes
CARICOM – Dominican Republic (1998)	Yes	Yes	Yes	Yes*	Future	No	Separate chapter	Yes
CARIFORUM – European Community (2008)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
Central American Economic Integration	Not specified	No general article	No	No	No	No	No	Not specified
EU (1957)	Yes	Yes	Yes	Yes	No	Yes (covered	Yes	Yes

Agreements	MFN Treatment	National Treatment	Market access (N-D QRs)+	Domestic Regulation	Emergency Safeguards	Subsidy Disciplines	Government procurement	Rule of origin (denial of benefits)
						under competition disciplines)		
Europe Agreements	Yes	Yes	No	Yes	No	Yes (covered under competition disciplines)	No	Beneficiaries specified through definition of “undertakings”
EU-México (1997)	Yes	Yes	Yes	No (provisions on regulatory carve-out and recognition)	No	No	Separate chapter	Yes
EFTA – Colombia (2008)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
EFTA – Co-operation Council for the Arab States of the Gulf (2009)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
EFTA – México (2000)	Yes	Yes	Yes	Yes	No	No	No	Not specified
EFTA-Singapore (2002)	Yes	Yes	Yes	Yes	No	Requests for consultations to be given sympathetic consideration	Separate chapter	Yes
China – ASEAN	No	Yes	Yes	Yes	No	No	No	Yes

Agreements	MFN Treatment	National Treatment	Market access (N-D QRs)+	Domestic Regulation	Emergency Safeguards	Subsidy Disciplines	Government procurement	Rule of origin (denial of benefits)
(2007)								
China – Singapore (2008)	No	Yes	Yes	Yes	No	No	No	Yes
India – Korea (2009)	Consideration to be given to request for MFN treatment	Yes	Yes	Yes	No	No	No	Yes
India – Singapore (2005)	Consideration to be given to request for MFN treatment	Yes	Yes	Yes	No	No	No	Yes
Japan – Chile (2007)	Yes	Yes	No (only in relation to financial services)	Yes	No	No	Separate chapter	Yes
Japan – Indonesia (2007)	Yes	Yes	Yes	Yes	No	No	No	Yes
Japan – Malaysia (2005)	Yes	Yes	Yes	Yes	Future	No	No	Yes
Japan – Philippines (2006)	Yes	Yes	Yes	Yes	No	No	Future	Yes
Japan – Singapore (2002)	No	Yes	Yes	Yes	No	No	Separate chapter	Yes
Japan – Switzerland (2009)	Yes	Yes	Yes	Yes	No	No	No	Yes
Japan –Thailand	Yes	Yes	Yes	Yes	Future	No	No	Yes

Agreements	MFN Treatment	National Treatment	Market access (N-D QRs)+	Domestic Regulation	Emergency Safeguards	Subsidy Disciplines	Government procurement	Rule of origin (denial of benefits)
(2007)								
Korea – Singapore (2005)		Yes	Yes	Yes	No	No	Separate chapter	Yes
Malaysia – Pakistan 2007)	Yes	Yes	Yes	Yes	Future	No	No	Yes
Singapore – Panama (2006)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
Singapore – Jordan (2005)	No	Yes	Yes	Yes	No	No	No	Yes
Taiwan – Nicaragua (2006)	Yes	Yes	Yes	Yes	No	No	No	Yes
ASEAN Framework Agreement on Services (1995)	Yes	Yes	Yes	Not specified	Yes	No	No	Yes
ASEAN- Australia (2009)	Consideration on request	Yes	Yes	Yes	No	No	No	Yes
Australia – New Zealand Closer Economic Relations Trade Agreement (1988)	MFN for excluded sectors	Yes	Yes	Yes	No	Export subsidies prohibited Other subsidies excluded	No	Yes
New Zealand – China (2008)	Yes	Yes	Yes	Yes	No	No	No	Yes
US – Jordan (2000)	Yes	Yes	Yes	Yes	No	Future negotiations	Yes	Yes
US-Singapore	Yes	Yes	Yes	Yes*	No	No	Separate	Yes

Agreements	MFN Treatment	National Treatment	Market access (N-D QRs)+	Domestic Regulation	Emergency Safeguards	Subsidy Disciplines	Government procurement	Rule of origin (denial of benefits)
(2003)							chapter	
US-Chile (2003)	Yes	Yes	Yes	Yes*	No	No	Separate chapter	Yes
US- Colombia (2006)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
US – Oman (2006)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes
US-Panama (2007)	Yes	Yes	Yes	Yes	No	No	Separate chapter	Yes

+ Non-discriminatory quantitative restrictions

* Rules on domestic regulation are set out more narrowly (in most cases they apply only to the licensing and certification of professional services suppliers)

[1] Honduras, Guatemala and El Salvador

Lesser convergence (and more limited PTA progress) can be observed in areas of rule-making that have posed recurring difficulties in the GATS setting. This includes issues such as domestic regulation, emergency safeguards and subsidy disciplines for services.

Most-favored nation and national treatment

The principles of most-favored nation and national treatment constitute two of the most basic building blocks to any agreement on services, just as they do in the goods area. As with the GATS, very few PTAs set out such principles in unqualified form[5], regardless of whether they are framed as general obligations (which is the case for MFN in virtually all agreements and for national treatment in agreements pursuing a negative list approach to liberalization) or as obligations that apply solely in sectors where liberalization commitments are positively undertaken.

While one can easily understand why MFN is required within agreements that imply more than two Parties, so as to ensure an equality of preferential treatment among all signatories, the question arises of why an MFN obligation should be embedded in PTAs concluded among bilateral partners. Part of the reason lies in the policy interest, first addressed in the NAFTA, for members of a given PTA to automatically secure any PTA+ benefits that any one Party to the original PTA may be willing to accord to a third Party in a subsequent PTA. In the case of NAFTA, for instance, any NAFTA+ commitment that say Canada or Mexico might be willing to grant to the European Union in the context of a subsequent PTA would need to be granted to the United States. The issue of MFN treatment in service sector PTAs has generated much policy controversy in the context of the Economic Partnership Agreements that the member States of the European Union have entered into with the CARIFORUM countries and plan to conclude with other ACP country groupings[6], with fears expressed that such a clause (which would only apply to agreements involving partners accounting for more than 1% of world trade) could reduce incentives for South-South PTAs in services if the benefits of such integration would automatically flow (for free) to EU members. Such a debate seems to have eschewed one important political economy consideration – that third country MFN rights allow smaller countries to benefit from the negotiating clout of larger partners that sign agreements with common partners.[7]

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[5] Only the Mercosul Protocol and Decision 439 of the Andean Community provide that no deviation from MFN and national treatment be allowed among members to the two integration groupings.

[6] For a fuller discussion of the issue of MFN treatment in EU-ACP EPAs, see Messerlin (2009).

[7] For a fuller discussion, see Baldwin, Evenett and Low (2009).

A weaker variation on the above discussion can be found in the recently concluded India- Korea FTA, which stipulates that if any party subsequently enters into another agreement which offers more favorable treatment to a non-party, then that party is to give consideration to a request by the other party for the incorporation of such treatment into the PTA. Any such incorporation should maintain the balance of concessions in the overall agreement.[8] Similarly, in the ASEAN–Australia–New Zealand (AANZ) FTA, if any more favorable treatment is granted in a future trade agreement by one party to a non party to the AANZ FTA, then the other parties to the AANZ FTA may request consultations to discuss the possibility of extending no less favorable treatment.[9]. In addition, the requested party shall enter into consultations with the requesting party bearing in mind the overall balance of benefits.[10]

Transparency

As may be expected given the regulatory intensity of services trade, transparency disciplines are common to all PTAs covering services. These typically stipulate, as is the case under GATS, an obligation to publish relevant measures and notify new (or changes to existing) measures affecting trade in services and to establish national enquiry points to provide information on measures affecting services trade upon request. One innovation over the GATS is the provision that some PTAs make for members to afford the opportunity (to the extent possible, i.e. on a "best endeavors" basis) for prior comment on proposed changes to services regulations. Increasingly, such provisions are becoming legally binding. This is most notably the case in North-South PTAs, following a trend initiated by the US-Chile and US-Singapore FTAs. The latter development offers an interesting example of what could be described as "tactical" or "demonstration effect" regionalism, with advances at the PTA level creating precedents whose proponents hope will facilitate their subsequent replication at the multilateral level.[11]

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[8] Comprehensive Economic Partnership Agreement between the Republic of Korea and the Republic of India, Article 6.3.

[9] Agreement Establishing the ASEAN–Australia–New Zealand Free Trade Area, Chapter 8, Article 7.

[10] Furthermore, there is a measure of asymmetry in this provision as the obligation does not apply to bilateral or plurilateral agreements between an ASEAN state or the ASEAN states on the one hand and a non- party or Australia or New Zealand on the other.

[11] Other examples of demonstration effect/precedent-setting regionalism are the provisions on the linkages between trade and labor standards inserted in the waning days of the Clinton administration into the US-Jordan FTA and the recurring tendency of the European

Market access

While PTAs covering services typically address non-discriminatory quantitative restrictions that impede access to services markets (addressed in part under Article XVI of the GATS), a number of earlier PTAs, particularly those concluded in the Western Hemisphere and modeled on the NAFTA, were actually weaker than the GATS, committing parties solely to making such measures fully transparent in annexes listing non-conforming measures and to a best endeavors approach as regards their progressive dismantling in future. In contrast, under GATS, WTO members undertake policy bindings in sectors, sub-sectors and modes of supply against which market access commitments are scheduled. Such a WTO-minus provision is no longer found in the newest generation PTAs entered into by the United States, Canada and others that had initially agreed to such a standard of treatment. Such a provision has been replaced by language such as that found early on in MERCOSUL and in the various PTAs to which EU Members are party, that introduce a prohibition on the introduction of new non-discriminatory QRs on any scheduled commitment and sector, mirroring a similar requirement under Article XVI of the GATS.

Domestic regulation

As discussed above, the argument has been made that PTAs in the services field provide scope for creating "optimum regulatory areas", the presumption being that the aggregate adjustment costs of regulatory convergence and policy harmonization are likely to be smaller when foreign regulatory preferences are similar and regulatory institutions broadly compatible. Both sets of conditions are likelier on balance to obtain among countries that are "closer" in physical, linguistic, cultural or historical terms (Mattoo and Fink, 2002). In practice, however, it is notable how the broad intersect between domestic regulation and services trade has tended to prove intractable (just as it has under the GATS) even among the smaller subset of countries engaging in PTAs.

In many instances, PTAs address domestic regulation in a manner analogous to that found in Article VI of the GATS, i.e. with a focus on procedural transparency and ensuring that regulatory activity does not lead to unduly burdensome or disguised restrictions to trade or investment in services. With the exception of the EU itself and of agreements reached between the EU and countries in Central and Eastern Europe

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Commission to insert disciplines on trade and competition into the EU's PTAs with developing countries.

in pre-EU accession mode, no PTA has to date made tangible progress in delineating the possible elements of a necessity test aimed at ensuring broad proportionality between regulatory means and objectives (as is potentially foreseen under the GATS' Article VI:4 mandate).[12]

It is notable that neither the NAFTA nor the many NAFTA-type agreements reached in the Western Hemisphere contain an article on domestic regulation *per se* in their services chapters. Rather, such agreements feature more narrowly drawn disciplines relating to the licensing and certification of professionals.[13]
On most matters relating to rules governing domestic regulation in services trade, progress has indeed been greater at the multilateral than at the PTA level. . Such progress has been evident in the Doha Round discussions on licensing requirements and procedures, qualification requirements and procedures and technical standards, transparency and special and differential treatment. Indeed, the disciplines on licensing procedures found in a number of recent PTAs entered into by some of the members of the 'Friends of Domestic Regulation' (the main *demandeurs* for domestic regulation disciples at the multilateral level) reflect the progress made in the Doha Round negotiations. For instance, in the China-Singapore FTA, Article 65:3(a) makes specific provision for applicants to remedy deficiencies in their applications. In addition, in cases where an application was either denied or terminated, the applicant is afforded the possibility of resubmitting a new application at its discretion.[14] Similar provisions are found in Article 10:5 of the AANZ FTA and Article 111:3 of the New Zealand – China FTA. Although the above provisions on licensing procedures in these PTAs do not go as far as the draft Doha Round proposals , they offer an interesting illustration of the iterative relationship between PTAs and the WTO and of the way in which PTAs can reverse engineer developments originating at the multilateral level. The area of domestic regulation is one in which an increasing number of PTAs embed existing GATS provisions and signal the desire of Members to incorporate by reference the ultimate outcome of the ongoing GATS Article VI:4 negotiating mandate. In so doing, PTAs cease to assume the role of rule-making laboratories, a trend that is most common in regard to the "unfinished agenda" of GATS (with the notable exception of government procurement).

[12] See Delimatsis (2008) for a fuller depiction of the state of play of GATS discussions under the Article VI:4 work program.

[13] Whereas similar GATS language states that the measures in question should not be a restriction to the supply of a service under any of the four GATS modes, the NAFTA-type agreements narrow this requirement to the cross-border supply of a service. No comparable provision can be found in these agreements' investment chapters.

[14] China-Singapore Free Trade Agreement, Article 65:3(c).

Harmonization, mutual recognition and regulatory cooperation

With a few notable exceptions, notably the EU and ANZCEPTA, both of which involve a level of integration that extends to a common labor market, tangible progress on matters of regulatory harmonization or mutual recognition within PTAs has generally proven more arduous than might be expected in theory (see Box 2).

Box 2. Harmonization and Mutual Recognition in Services: Promise and Pitfalls

The pessimism that calls for regulatory harmonization often generates is based on the absence of widely accepted international standards in services. Where such standards do exist, as in financial services or maritime transport, meeting them tends to be seen as a first step towards acceptability, rather than as a sufficient condition for market access. The GATS, like the GATT, does not specifically require the use of international standards. It generally provides weaker incentives for the use of such standards than the SPS or the TBT Agreements, and does not provide a presumption of compliance as do the latter two agreements.[15]

It is unlikely that meaningful international standards for most services will be developed soon. Still, it bears noting that in those areas where global standards do exist, the likelihood of disguised or needlessly restrictive impediments to trade and investment may be significantly lower, even as overtly discriminatory regulatory barriers or market access impediments subject to Articles XVI (Market Access) and XVII (National Treatment) (and typically "reserved" in scheduled sectors) may remain in place. The presumption must also be that the existence of such standards may significantly facilitate trade (particularly cross-border trade by helping overcome the various forms of information asymmetries that hold such trade – and its commensurate liberalization under GATS- back) and investment.

Accordingly, efforts should be directed to ensuring that trade agreements create a stronger presumption in favor of genuinely international standards in services trade. As with recognition agreements, efforts at developing international standards for services trade will likely require greater doses of technical assistance and capacity building. This may be usefully done at the

[15] Such a presumption can be found in Article 2.5 of the TBT Agreement and Article 3.2 of the SPS Agreement.

national and regional levels, particularly as proximity, both geographic historical, and cultural, may be expected to facilitate regulatory convergence.

Efforts to promote the adoption of international standards will invariably be carried out outside a trade policy framework. Contrary to much popular belief, trade agreements are not in the business of making regulatory standards. Rather, their remit lies in how such standards are implemented *if* they impact on trade. The relevant institutions for promoting international standards for services are to be found in various specialized regulatory institutions, such as the Bank for International Settlements for banking standards, the International Telecommunications Union for telecommunications or the International Standardization Organization (ISO) for various categories of services (including the means of producing and supplying them).[16]

As regards mutual recognition agreements (MRAs), three observations seem in order. First, they cannot be made to happen. Secondly, they do not seem to be happening – at least not on any major trade-influencing scale and certainly not at the multilateral level. Often touted as a desirable transaction cost-reducing alternative to regulatory harmonization, there are in practice relatively few examples of successful, operative MRAs in services trade.[17] Thirdly, even if MRAs were to happen in greater numbers, it is unclear whether they would always be desirable.

A multilateral agreement like the GATS cannot mandate countries to conclude MRAs – just as any provision such as Article V of GATS (Economic Integration) or Article XXIV of GATT cannot make regional integration agreements happen. As in the case of regional agreements, multilateral disciplines can be more or less permissive with regard to mutual recognition.

This in turn raises a key question: where and how strong are the incentives to conclude MRAs? The practice of MRAs suggests that their scope is often quite limited; they are invariably concluded between very similar countries. Even in a region with as strong an integrationist dynamic as Europe, and despite a significant level of prior and/or complementary (minimal) regulatory harmonization, the effect of MRAs has been limited by the unwillingness of

[16] One concrete example of forward movement in international standardisation involving developing countries is provided by the IMF-World Bank Comprehensive Financial Sector Adjustment Programs, which are helping many jurisdictions to assess their compliance with international standards in the financial sector with the aim to help them address any underlying weaknesses. Carried out on a voluntary basis outside of the trade policy framework, such regulatory cooperation may nonetheless be expected to facilitate the progressive, orderly, pursuit of liberalization of trade and investment in financial services.

[17] See Beviglia-Zampetti (2000). See also Nicolaidis and Trachtman (2000).

many host country regulators to cede full control. It should come as no surprise that MRAs have yet to exert significant effects on services trade.

Such an outcome in turn raises the question of the benefits and costs of MRAs. The analogy with regional integration agreements is here again useful, as MRAs can be likened to sector-specific preferential arrangements. In instances where regulatory barriers are prohibitively high - one can imagine autarky as the ultimate example - then recognition can only be trade creating. But if they are not, then selective recognition can have discriminatory effects and lead to trade diversion. The result may well be to create trade according to a pattern of mutual trust rather than on the basis of the forces of comparative advantage. For instance, one can readily observe OECD countries making progress (albeit limited) towards MRAs in professional services, but avoiding such agreements with countries such as India, Egypt or the Philippines.

Article VII (Recognition) of the GATS strikes a delicate balance by allowing such agreements, provided third countries have the opportunity to accede or demonstrate equivalence. Thus, Article VII has a desirable open-ended aspect that Article V (dealing with integration agreements) does not. This makes it particularly worrisome that many MRAs have been notified by WTO Members under Article V rather than VII. In any case, the key concern for any multilateral agreement should be not how those who enjoy preferential access are treated, but how those who do not enjoy such access are treated. Ironically, the only line of defense of the rights of third countries could well come from a necessity test aimed at ensuring that such countries would not be subject to unnecessarily burdensome regulation even if they were not parties to an MRA.

Because of the potential of MRAs to create trade and investment distortions, bilateral or plurilateral recognition agreements should respect the non-discrimination principle, as mandated by Article VII of GATS. Such agreements should not, as a rule, be notified under Article V of GATS (Economic Integration) but rather be open to all eligible participants under the terms of Article VII.

Source: Mattoo and Sauvé (2003).

Moreover, even though a number of PTAs call on Members to recognize, at times on the basis of explicit timetables , foreign educational credentials and professional qualifications in selected professions, progress in concluding mutual recognition agreements has often proven slow, difficult, and partial. This is particularly noteworthy of agreements pursued between countries with federal political regimes and systems of delegated authority to licensing bodies at the sub-national level.

Still, compared with progress registered under Article VII (Recognition) of the GATS, reliance on the subsidiary approaches afforded by PTAs has allowed some degree of tangible progress. Such advances appear more pronounced within South-South PTAs such as Mercosul and ASEAN's Framework Agreement on Services (AFAS), both of which have seen the conclusion of mutual recognition agreements in several regulated professions (e.g. nurses, engineers, accountants, architects, lawyers).

Most PTAs feature provisions calling for greater institutional cooperation between domestic regulators of parties' in implementing agreements, typically setting up joint regulatory commissions and periodic meetings at senior or ministerial level. The benefits of such cooperation, even as it proceeds from soft law undertakings, can still yield important trade- and investment-facilitating benefits and help build trust, enhance enforcement capacities and identify post-negotiation implementation bottlenecks, all of which may be key ingredients – indeed pre-conditions - for regulatory harmonization and effective mutual recognition initiatives.

Emergency safeguard mechanisms, subsidy disciplines and government procurement

With few exceptions, PTAs have made little headway in tackling the key "unfinished" rule-making items on the GATS agenda. This is most notably the case for disciplines on an emergency safeguard mechanism (ESM) and subsidy disciplines for services trade, where governments confront the same conceptual challenges, data limitations, feasibility challenges and political sensitivities at the regional level as they do on the multilateral front. It bears noting for instance that the countries of Southeast Asia, which until recently counted amongst the most vocal proponents of an emergency safeguard mechanism in the GATS, have yet to adopt such a provision within their own ASEAN Framework Agreement on Services (AFAS) To date, only members of CARICOM (in Protocol II) in the Western Hemisphere, have adopted (but not yet used) such an instrument, and questions remain as to the operational feasibility and ultimate necessity of an ESM in services trade given the flexibilities embedded in the very conduct of market opening under most agreements.

The NAFTA has provided one example of sector-specific experimentation (in financial services) with safeguard-type measures. Under the terms of the NAFTA's chapter on financial services, Mexico was allowed to impose market share caps if the specific foreign ownership thresholds agreed to – 25 and 30 percent respectively for banks and securities firms – were reached before 2004. Under the terms of the agreement, Mexico could only have recourse to such market share limitations once during the 2000-2004 period and could only impose them for a three-year period. Under no circumstances could such measures be maintained beyond the end of the transition period foreseen for market opening under the NAFTA (e.g. 2001). It bears noting that Mexico never made use of such provisions even as the aggregate share

of foreign participation in its financial system became significantly higher than the thresholds described above (Sauvé, 2002; 2008; Sauvé and Gonzalez-Hermosillo, 1993). It is interesting, if somewhat surprising, that no further attempt has been made, either in PTAs or at the WTO level, to consider the scope for - and practical means of - replicating the Mexican financial services example on a sectoral basis in areas where market opening may be prone to unanticipated dislocations and have potentially injurious consequences for smaller domestic firms, as in distribution for instance. The quest for a generic emergency safeguard measure applicable to all sectors and predicated on the GATT model has led to a negotiating stalemate at both the PTA and WTO levels.[18]

On the issue of disciplines for service-related subsidies, once more with the exception of the EU (including its pre-accession agreements with countries in Central and Eastern Europe) and of ANZCEPTA, the quest for rule-making advances has proven just as elusive at the PTA than at the WTO level, particularly within countries with federal systems of governance given the extent of sub-national policy activism (and the concomitant reluctance to take on binding obligations) in this area.

Whereas a number of PTAs (e.g. MERCOSUL) replicate the call, made in GATS, to develop future disciplines on subsidies in services trade, the vast majority of PTAs covering services specifically exclude subsidy practices from their coverage. Paralleling provisions found in GATS, the EFTA-Singapore FTA requires that sympathetic consideration be given to requests by a party for consultations in instances where subsidy practices affecting trade in services may be deemed to have injurious effects. The area of subsidy disciplines, like that of domestic regulation, is one where many PTAs signal a desire to incorporate by reference the outcome of any agreed outcome from ongoing (but largely stagnant) discussions at the WTO level, where important points of discord continue to surround issues of definition and scope, considerations of likeness as well as the applicability and practical modalities of trade remedies in services trade.[19]

More progress has been made at the PTA level in opening up government procurement markets in services, though this has tended to be achieved through negotiations in the area of government procurement per se (as with the WTO's Government Procurement Agreement or GPA) rather than addressed in services negotiations.[20]

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[18] For a fuller discussion, see Sauvé (2002), Pierola (2008) and Marconini (2005).

[19] For a fuller discussion of the debate over subsidies in services trade, see Sauvé (2002), Poretti (2008), and Adlung (2007).

[20] Still, it bears recalling that despite notable progress in PTAs, government procurement practices continue in most instances to be the province of discriminatory practices. In the case of NAFTA, for instance, despite the fact that the scope of covered purchases was quadrupled when compared to the outcome of the 1987 Canada-United States FTA, covered

The approach taken in PTAs is for the most part very similar to that adopted in the WTO, i.e. non-discrimination among members within the scope of scheduled commitments and procedures to enhance transparency and due process. PTAs whose members are all parties to the GPA, such as EFTA and the Singapore–Japan FTA, specifically mention that the relevant GPA articles apply and most agreements concluded in the Western Hemisphere basically replicate GPA disciplines at the regional level. However, it bears noting that unlike the GPA, which applies in principle to purchases by both state and sub-national governments, the majority of PTAs provide for binding government procurement disciplines at the national level only (OECD, 2002a).[21]

Investment

One policy domain where PTAs have achieved considerable progress, both in terms of rule-making but also that of market opening, is that of investment rule-making, where forward movement has not proven possible to date in the WTO. Most PTAs feature comprehensive disciplines on the protection and liberalization of cross-border activity to which scope exists for investor-state arbitration alongside WTO-like state-to-state dispute settlement, together with extensive liberalization commitments, most often brokered on a negative list basis. Given the central role assumed by investment as the most important mode of service supply, such developments are of some significance for the operation of services markets and for promoting more contestable entry conditions in tem.[22] The extent to which PTAs featuring comprehensive investment norms might influence the WTO's evolving architecture of rules will very much depend on prospects for crafting a multilateral regime for investment. Any such agreement at the WTO level would likely raise a number of intractable questions regarding the scope of the GATS and notably its coverage of commercial presence as a mode of supplying services. Starting with the NAFTA in 1994, a large and growing number of PTAs have shown how the treatment of investment in services need not be distinguished from that in other sectors subject to trade

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entities only represented a tenth of North America's civilian procurement market at the time of the Agreement's entry into force. See Hart and Sauvé (1997).

[21] For a detailed discussion of the treatment of government procurement in PTAs, see the chapter by Dawar and Evenett in this volume.

[22] For a fuller discussion of the evolution of international rules on investment, see Beviglia-Zampetti and Sauvé (2007).

disciplines. The issue of preferential advances in investment rule-making is taken up by Sébastien Miroudot in Chapter X of this volume.

Rules of origin/denial of benefits

A final area of rule-making deserving attention in a discussion of PTAs and services trade concerns the issue of rules of origin. Such rules condition who ultimately qualifies for preferential treatment under PTAs. In services agreements, this matter is generally addressed under provisions dealing with denial of benefits.[23]

The literature on rules of origin has focused almost exclusively on merchandise trade flows and hence on policies for determining the origin or nationality of tangible *products*. Much less attention has been devoted to the increasingly important issue of how to determine the origin of *producers*, which is primarily what the study of rules of origin in services trade and investment is concerned with. Since contesting service markets often requires the physical presence of suppliers in the territory of consumers, either in the form of individual service providers performing cross-border transactions on a temporary (i.e. contract) basis or as entities servicing a foreign market on the basis of a commercial presence in that market, governments that are signatories of trade and investment agreements may need to ascertain whether suppliers originate in other countries, with a view to extending or denying the benefits foreseen under such agreements.

Experience shows that rules of origin for services and investment can play a significant role in determining the degree to which regional trading arrangements discriminate against non-member countries, and hence the extent of potentially costly trade and investment diversion. When levels of protection differ between participating countries, the effective preference granted to a trading partner will depend on how restrictive the applied rule of origin is. In the extreme, if one participant has a fully liberalized market, the adoption of a liberal rule of origin by the other participants can be likened to MFN liberalization, as services and service suppliers can enter or establish themselves in the liberal jurisdiction and from there move to – or service – the other partner countries.

From an efficiency perspective, the policy on origin rules for services should be to allow for third country service suppliers, particularly those operating through a commercial presence (e.g. via Mode 3 entry) to take advantage of –

[23] For a fuller discussion of rules of origin in services trade, see Beviglia-Zampetti and Sauvé, (2006)

and contribute to - the benefits of an integrating area. Under a liberal rule of origin for services and investment[24] aimed at ensuring that established foreign operators are not mere shell companies but conduct substantial business operations in the host country market, third country investors and service providers can take full advantage of the expanded market opportunities afforded by the creation of a PTA by establishing a commercial presence within the integration area. Not surprisingly, participants who seek to benefit from preferential access to a protected market and deny benefits to third country competitors are likely to argue for the adoption of restrictive rules of origin. This could be the attitude, in particular, of regionally dominant but non-globally competitive service providers towards third-country competition within a regionally integrating area.

The adoption of restrictive rules of origin are permissible under GATS Article V:3, which allows PTAs concluded between developing countries (i.e South-South PTAs) to restrict the benefits of integration to service suppliers that are owned and controlled by citizens of the integrating area. It is not clear whether such flexibility serves the development interests of those that use them. Several South-South PTAs, notably ASEAN, Mercosul, the Andean Pact, the China-Hong Kong or the China-Macau FTAs , have opted for a restrictive policy stance in this area.

The policy stance taken with regard to rules of origin for services and investment in a PTA can play an important role promoting or inhibiting access to the most efficient suppliers of services. In many service sectors, the most efficient (or globally competitive) suppliers will tend to be either developed country firms or firms originating outside an integrating area. Accordingly, the adoption of rules of origin that restrict benefits to nationals of member states can exert detrimental effects by potentially locking in integrating partners into sub-optimal patterns of production and consumption. The above problem may be compounded, and generate longer-term deadweight losses, to the extent that many services, particularly network-based services, involve significant location specific sunk costs, such that first movers (even if relatively inefficient) can exert long-term dominance and extract monopolistic rents. As discussed earlier, the problem with location-specific sunk costs is that a country may be stuck with inferior suppliers for a long time even if it subsequently liberalizes on an MFN basis. Indeed, because of the importance

[24] More restrictive rules of origin conditioning the receipt of preferences may relate to various factors, such as local incorporation (such that benefits are denied to branches of third country invested entities), place of incorporation or location of headquarters or ownership and control tests aimed at limiting PTA benefits to local juridical persons. Examples of the latter can be found under MERCOSUL or the Andean Pact.

of sunk costs in many service industries, sequential entry (which preferential liberalization with restrictive rules of origin can easily promote) can produce very different results from simultaneous entry. If entry is costly, an incumbent may indeed be able to fully deter entry, leading to greater market concentration and a reduction in consumer welfare.[25]
Some measure of solace can therefore be taken from the observation, confirmed in this chapter's sample of reviewed PTAs, that the vast majority of preferential agreements have to date adopted the most liberal rule of origin for Mode 3 suppliers, whereby any juridical person incorporated in any party to an integration agreement and conducting substantial business operations therein receives full treaty benefits.

2.2 Modalities of liberalization: negative vs. positive list approaches

Two major approaches towards the liberalization of trade and investment in services have been manifest in PTAs and in the WTO: the positive list or "bottom-up" approach (typically a hybrid approach featuring a voluntary, positive, choice of sectors, sub-sectors and/or modes of supply in which governments are willing to make binding commitments together with a negative list of non-conforming measures to be retained in scheduled areas), and the negative list or "top-down/list it or lose it" approach

While both negotiating modalities can be made to produce broadly equivalent outcomes in liberalization terms, the two approaches can be argued to generate a number of qualitative differences of potential significance from both a domestic and international governance point of view.[26]

While the debate over these competing approaches appears settled in the GATS context, it is useful to recall these differences as the issue is still very much alive in a PTA context and as WTO Members contemplate the scope that may exist in the current negotiations for making possible improvements to the GATS architecture.

Under a GATS-like, positive (or hybrid) approach to scheduling liberalization commitments, countries agree to undertake national treatment and market access

[25] For a fuller discussion, see Mattoo and Fink (2002).
[26] The purpose of the ensuing discussion is to note such differences without advocating any implicit hierarchy of policy desirability. Both approaches have strengths and weaknesses. The governance-enhancing aspects of negative listing have, however, been noted by several observers. See, in particular: Sauvé (1996); Snape and Bosworth (1996); World Trade Organization (2001); and Stephenson (2002). For a fuller discussion of the good governance promoting aspects of PTAs, see Baldwin, Evenett and Low (2009), as well as Chapter 1 of this volume.

commitments specifying (through reservations in scheduled areas) the nature of treatment or access offered to foreign services or foreign service suppliers.[27] Under such an approach, countries retain the full right to undertake no commitments. In such instances, they are under no legal obligation to supply information to their trading partners on the nature of discriminatory or access-impeding regulations maintained at the domestic level.

A related feature of the GATS that tends to be replicated in PTAs that espouse a bottom-up (hybrid) approach to liberalization is to afford countries the possibility of making commitments that do not reflect (i.e. are made below) the regulatory *status quo* (a long-standing practice in tariff negotiations that was replicated in a GATS setting).

The alternative, "top-down" approach to services trade and investment liberalization is based upon the concept of negative listing, whereby all sectors and non-conforming measures are to be liberalized unless otherwise specified in a transparent manner in reservation lists appended to an agreement. Non-conforming measures contained in reservation lists are then usually liberalized through consultations or, as in the GATS, periodic negotiations.

It is interesting to note that despite the strong opposition that such an approach generated when first mooted by a few GATT Contracting Parties during the Uruguay Round, the negative list approach to services liberalization has in recent years been adopted in a majority of PTAs covering services that have been notified to the WTO to date. In the sample of 55 PTAs under review in this chapter, 33 follow a negative list approach (60% of the total).

First used (for trade in services only in the absence of an investment chapter) by Australia and New Zealand in ANZCEPTA, the approach was further developed by Canada, Mexico and the United States under NAFTA in 1994. Since the NAFTA took effect, Mexico played a pivotal role in extending this liberalization approach and similar types of disciplines (i.e. right of non-establishment) on services to other PTAs it has signed with countries in South and Central America.[28]

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[27] Members of MERCOSUL adopted one slightly different version of the positive list approach with a view to liberalising services trade within the region. According to MERCOSUL's Protocol of Montevideo on Trade in Services, annual rounds of negotiations based on the scheduling of increasing numbers of commitments in all sectors (with no exclusions) are to result in the elimination of all restrictions to services trade among the members of the group within ten years of the entry into force of the Protocol. The latter has yet to enter into force. See Stephenson (2001) and Pena (2000).

[28] The Andean Community has adopted a somewhat different version of the negative list approach. Decision 439 on Trade in Services specifies that the process of liberalization is to begin when comprehensive (non-binding) national inventories of measures affecting trade in services for all members of the Andean Community are finalized. Discriminatory restrictions listed in these inventories are to be lifted gradually through a series of negotiations, ultimately

This pattern has been replicated in PTAs signed between Central and South American countries on one hand and Asian countries on the other hand, particularly those involving the region's most advanced partners, among which Japan, South Korea, Australia, New Zealand and Singapore and Chinese Taipei.

A number of distinguishing features of negative listing can be identified. For one, such an approach enshrines and affirms the up-front commitment of signatories (subject to reservations) to an overarching set of general obligations. This is currently the case under the GATS primarily with respect to the Agreement's provisions on MFN treatment (Article II, with scope for one-time exceptions) and transparency (Article III), with most other disciplines applying in an à la carte manner to sectors and modes of supply on those terms inscribed in members' schedules of commitments.[29]

A second, and perhaps more immediately operational, defining characteristic of negative listing lies in its ability to generate a standstill, i.e. to establish a stronger floor of liberalization by locking-in the statutory or regulatory *status quo.* Such an approach therefore avoids the GATS pitfall of allowing a wedge to arise between applied and bound regulatory or statutory practices.[30] An important caveat however lies in the propensity of negative list agreements to allow Parties to lodge reservations that preserve future regulatory freedom in a manner analogous to "unbound" or non-scheduled commitments under the GATS. Here again, however, and unlike the GATS which yields no information on the nature of non-conforming measures retained in what are typically sensitive sectors, negative list agreements oblige signatories to reveal the nature of existing non-conforming measures in such reserved sectors.

The main governance-enhancing feature arising from the adoption of a negative list approach is thus the greater level of transparency it can generate if adhered to

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resulting in a common market free of barriers to services trade within a five-year period set out to conclude in 2005.

[29] It bears noting however that most PTAs that employ a negative list approach to liberalization feature so-called "unbound" reservations, listing sectors in which Members wish to preserve the right to introduce new non-conforming measures in future. In many PTAs, particularly those modeled on the NAFTA, such reservations nonetheless oblige member countries to list existing discriminatory or access-impairing measures whose effect on foreign services or service suppliers might in future be made more burdensome.

[30] The suggestion has been made that WTO Members could address this issue in GATS without revisiting the Agreement's negotiating modality by agreeing to a new framework provision whose purpose would be to encourage governments to reflect the statutory or regulatory *status quo* in their scheduled commitments (whilst keeping with the voluntary nature of such commitments). See Sauvé and Wilkie (2000).

properly[31] The information contained in reservation lists will be important to prospective traders and investors, who value the one-stop shopping attributes of a comprehensive inventory of potential restrictions in foreign markets. Such an inventory is also likely to benefit home country negotiators, assisting them in establishing a hierarchy of impediments to tackle in future negotiations. Such information can in turn lend itself more easily to formula-based liberalization, for instance by encouraging members to agree to reduce or progressively phase out "revealed" non-conforming measures that may be similar across countries (e.g. quantitative limitations on foreign ownership in selected sectors).[32]

The production of a negative list may also helps to generate a useful domestic policy dialogue between the trade negotiating and regulatory communities, thereby encouraging countries to perform a comprehensive audit of existing trade- and investment-restrictive measures, benchmark domestic regulatory regimes against best international practices, and revisit the rationale for, and most efficient means of satisfying, domestic policy objectives.[33]

A further liberalizing feature found in a number of PTAs using a negative list approach to liberalization consists of a ratchet mechanism (Table 2), whereby any autonomous liberalization measure undertaken by an PTA member between periodic negotiating rounds is automatically reflected in that member's schedule of commitments or lists of reservations. Such a provision typically aims at preventing countries from backsliding with respect to autonomously decreed policy changes. It may also facilitate the provision of negotiating credit for autonomous liberalization, an issue currently under discussion in the GATS context.

Such provisions are found in many PTAs concluded in the Western Hemisphere where, besides the NAFTA, it has been adopted in several PTAs covering services and concluded between developing countries. For instance, Article 10 of Andean Community Decision 439 on Services applies to all new measures affecting trade in services adopted by member countries and does not allow for the establishment of new measures that would increase the degree of non-conformity or fail to comply with the commitments contained in Article 6 (market access) and Article 8 (national treatment) of the Decision. Article 36 of the CARICOM Protocol is also a 'status quo'

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[31] This caveat is important as a number of PTAs, particularly those conducted along North-South lines, have seen powerful partners reserve all measures of a sub-national nature through one sweeping reservation that yields no information on the nature and sectoral incidence of non-conforming measures maintained by sub-national governments. Such reservations also greatly reduce the potential scope of the PTA in question to the extent that in many federal countries, important pockets of services regulation apply at the sub-national level. The insurance sector is the United States, or many energy-related services in Canada, are cases in point.

[32] See Sauvé (1996), *op. cit.*

[33] For a fuller discussion of the modalities and uses to which a trade-related regulatory audit may be put, see Sauvé (forthcoming) and Sauvé and Marconini (2009).

or standstill provision, prohibiting members from introducing any new restrictions on the provision of services in the Community by CARICOM nationals.

A provision of this type can exert positive effects on the investment climate of host countries by signaling to foreign suppliers the latter countries' commitment not to reverse the liberalizing course of policy change.[34] Such credibility-enhancing provisions may be especially important for smaller countries that often find it difficult to attract larger doses of foreign direct investment (FDI).

A recent comprehensive review of East Asian PTA commitments in services suggests that some qualification is required for the often-held belief that negative listing yields inherently greater transparency.[35] Some agreements using negative listing provide a clearer road map of existing regulatory impediments, whereas others fall short of expected transparency because, as noted above, they use sweeping sectoral or mode-specific carve-outs or exclude entire categories of measures (such as sub-national measures).[36]
Evidence on the impact of negative listing on induced levels of liberalization is also mixed. Some parties have reached hybrid list agreements that achieve greater liberalization than their negative list agreements with other partners. For example, Singapore's positively listed commitments in its PTA with Japan provide significantly greater coverage than its negatively listed commitments in its PTA with Australia. However, there is little doubt that done properly, negative list agreements may yield important benefits in regulatory transparency and by locking in the regulatory status quo.
Two potential pitfalls arising from the use of negative listing can however be identified. First, that such an approach may be administratively burdensome, particularly for developing countries. Such a burden may however be mitigated by allowing for progressivity in the completion of members' negative lists of non-conforming measures.[37] The costs of compliance must also be weighted against some of the benefits in governance and best regulatory practices described above.

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[34] See Hoekman and Sauvé (1994) and Stephenson (2001a).

[35] See Fink, C. and M. Molinuevo. 2007.

[36] One troubling example stems from recent PTA practice by the United States, which increasingly uses sweeping negative list reservations that exclude all measures affecting services at the sub-national level. Recent US PTAs are also notable for excluding Mode 4 commitments.

[40] In the NAFTA, for instance, sub-national governments were initially given an extra two years to complete their lists of non-conforming measures pertaining to services and investment. The NAFTA parties subsequently decided not to complete the lists at the sub-national level, opting instead for a standstill on existing non-conforming measures. Compliance with the production of negative lists has similarly been problematic elsewhere in the Western Hemisphere, as a number of agreements were concluded without such lists being finalized and without firm deadlines for doing so. The inability of "users" to access the

A second concern relates to the fact that the adoption of a negative list implies that governments ultimately forgo the right to introduce discriminatory or access-impairing measures in future, including in sectors that do not exist or are not regulated at the time of an agreement's entry into force.

Table 2. Comparing negotiating approaches in services trade

Type of approach/ Main features	**GATS-like (hybrid approach)**	**Negative list approach**
General description	Schedule of commitments *positively* list sectors, sub-sectors and/or modes of supply in which commitments on market access, national treatment as well as any additional commitments are undertaken and *negatively* lists any non-conforming treatment or measures retained therein. *A la carte* liberalization – members retain the right to choose sectors, sub-sectors and modes of supply in which they are prepared to undertake legally-binding market access, national treatment and any other additional commitments.	Free trade and investment in services is assumed unless specific *existing* measures are inscribed in reservation lists indicating the sector, sub-sector, industrial classification, nature of the treaty provision that is violated, description of the measure in question and the nature of the measure's non-conformity with regard to specific treaty provisions. List or lose – all non-conforming measures not notified at the moment of a PTA's entry into force are automatically bound at "free" (i.e. signatories lose the right to invoke non-conforming measures that are not inscribed in their lists of reservations upon an agreement's entry into force).
Locking in the regulatory *status*	Not guaranteed unless otherwise specified.	Generally guaranteed.

information contained in the negative lists to such agreements deprives the latter of an important good-governance promoting feature.

quo	Members are typically allowed to schedule commitments below the regulatory *status quo*, regardless of the level of market openness flowing from existing domestic regulatory measures.	
Transparency	Generally more limited as signatories retain the flexibility not to schedule commitments or to schedule commitments below the regulatory *status quo.*	Generally greater given focus on reserving existing non-conforming measures, but some agreements allow signatories to lodge sweeping reservations (e.g. all non-confirming measures maintained at the sub-national level).
Scope for introducing future non-conforming measures	Can be secured by either leaving a sector, sub-sector or mode of supply out of a member's schedule of commitments or by scheduling an "unbound" commitment. No information on the nature of non-conforming measures is generated in non-scheduled or unbound sectors, sub-sectors or modes of supply.	Specific annexes allow signatories to a negative list PTA to retain future policy flexibility in sectors, sub-sectors or modes of supply. These become the GATS equivalent of unbound measures. Parties are normally required to describe the current level of non-conformity prevailing in such reserved areas.
Ratchet mechanism	None	Many negative list PTAs feature a ratchet provision aimed at ensuring that any autonomous measure of a liberalizing nature enacted *after* a PTA's entry into force or, where envisaged, between periodic negotiating rounds, becomes the liberalizing party's commitment under the PTA, with market opening benefits automatically

		extended to PTA partners.on an MFN basis in the case of plurilaueral PTAs)

To assuage the latter concerns whilst promoting the transparency-enhancing properties associated with the use of negative listing, the suggestion has been made to encourage countries (including possibly in the WTO context) to exchange (as they have in the Andean Community and are considering doing within MERCOSUL) comprehensive (and non-binding) lists of non-conforming measures.[38]

In an important new development along the above lines, exemplified in the most recent Japanese PTAs, negotiators have sought to secure the best properties of negative and hybrid listing. Recent Japanese PTAs thus maintain a GATS-like hybrid approach to scheduling, preserving the right of countries to pick and choose those sectors, subsectors, and modes of supply in which they desire to make commitments. At the same time, the country's PTAs balance this flexibility with the twin obligations to schedule the regulatory *status quo* (that is, there is no GATS-like right to schedule commitments that offer less access than that which exists under the scheduling country's current laws and regulations) and to exchange non-binding lists of non-conforming measures (that is, a nonbinding negative list of trade and investment restrictions in all sectors is embedded in the PTA) so as to promote greater regulatory transparency. The EU-CARIFORUM EPA took a similar approach in allowing parties to schedule *status quo* commitments on a GATS basis.[39]

It bears noting, finally, that PTAs have becoming more flexible and important variations are being introduced depending on the negotiating partners. For instance, some of Japan's PTAs (with Indonesia, Malaysia, the Philippines and Thailand) have been conducted along positive list lines, while others take a negative list approach (with Chile and Switzerland). PTAs also increasingly mix positive and negative list approaches under the same agreement. Recourse to negative listing is particularly pronounced in the investment area, whereas some agreements use both approaches depending on the sector or mode of supply (e.g. positive listing for cross-border trade and negative listing for commercial presence; or negative listing for banking services and positive listing for insurance services).

[38] See Sauvé and Wilkie (2000) for a fuller depiction of such a proposal.

[39] For a fuller discussion, see Sauvé and Ward (2009), World Bank (2009) and ADB (2009).

Table 3: Key features of PTAs covering services

Agreements	Scope/ Coverage	Negotiating modality	Treatment of investment in services	Right of non establishment	Ratchet mechanism
GATS	Universal*	Positive list approach	Covered as "commercial presence" (mode 3)	No	No
NAFTA	Universal*	Negative list approach	Separate chapter	Yes	Yes
Canada – Chile	Universal*	Negative list approach	Separate chapter	Yes	Yes
Canada – Colombia	Universal*	Negative list approach	Separate chapter	Yes	Yes
Canada – Peru	Universal*	Negative list approach	Separate chapter	Yes	Yes
Chile – Mexico	Universal*	Negative list approach	Separate chapter	Yes	Yes
Bolivia-Mexico	Universal*	Negative list approach	Separate chapter	Yes	Yes
Costa Rica - Mexico	Universal*	Negative list approach	Separate chapter	Yes	Yes
Mexico – Nicaragua	Universal*	Negative list approach	Separate chapter	Yes	Yes
Mexico – Northern Triangle[1]	Universal*	Negative list approach	Separate chapter	Yes	Yes
Central America – Dominican Republic	Universal*	Negative list approach	Separate chapter	Yes	Yes
Central America – Dominican Republic – US	Universal*	Negative list approach	Separate chapter	Yes	Yes

Agreements	Scope/ Coverage	Negotiating modality	Treatment of investment in services	Right of non establishment	Ratchet mechanism
Central America – Chile	Universal*	Negative list approach	Separate chapter	Yes	Yes
Chile- Colombia	Universal*	Negative list approach	Separate chapter	Yes	Yes
El Salvador – Taiwan	Universal*	Negative list approach	Separate chapter	Yes	Yes
Guatemala - Taiwan	Universal*	Negative list approach	Separate chapter	Yes	Yes
Group of Three	Universal*	Negative list approach	Separate chapter	Yes	Yes
MERCOSUR	Universal*	Positive list approach	Separate Protocols	No	No
Andean Community	Universal*	Negative list approach	Covered as “commercial presence”	No	No
CARICOM	Universal*	Negative list approach	Covered as “commercial presence” and in separate chapters (on right of establishment and movement of capital)	No	No
CARICOM – Dominican Republic	Universal*	Negative list approach	Separate chapter	Yes	No
CARIFORUM – European Community	Universal* (audio-visual services explicitly excluded)	Positive list approach	Covered as “commercial presence”	No	No
Central American Common Market	Construction services	Positive list approach	Not specified	No	No

Agreements	Scope/ Coverage	Negotiating modality	Treatment of investment in services	Right of non establishment	Ratchet mechanism
EU	Universal*	Negative list approach	Treated as freedom to establish	Yes	No
Europe Agreements	Universal*	Negative list approach	Separate chapter	Yes	No
EU-Mexico	Universal* (audio-visual services explicitly excluded)	Standstill (+ future negotiation of commitments à la GATS)	Covered as "commercial presence" and under a separate investment chapter	No	No
EFTA – Mexico	Universal *	Positive list approach	Covered as "commercial presence" and under a separate investment chapter	No	No
EFTA – Colombia	Universal*	Positive list approach	Covered as "commercial presence"	No	No
EFTA – Co-operation Council for the Arab States of the Gulf	Universal*	Positive list approach	Covered as "commercial presence"	No	No
EFTA – Singapore	Universal*	Positive list approach	Covered as "commercial presence" and under a separate investment chapter	No	No
China – ASEAN	Universal	Positive list approach	Covered as "commercial presence"	No	No
China – Singapore	Universal*	Positive list approach	Covered as "commercial presence"	No	No
India – Korea	Universal*	Positive list approach	Covered as "commercial presence" and under a separate investment chapter	No	No
India – Singapore	Universal*	Positive list approach	Covered as "commercial presence"	No	No

Agreements	Scope/ Coverage	Negotiating modality	Treatment of investment in services	Right of non establishment	Ratchet mechanism
Japan – Chile	Universal*	Negative list approach	Separate chapter	Yes	Yes
Japan – Indonesia	Universal*	Positive list approach	Covered as “commercial presence” and under a separate investment chapter	No	No
Japan – Malaysia	Universal*	Positive list approach	Covered as “commercial presence” and under a separate investment chapter	No	No
Japan – Philippines	Universal*	Positive list approach	Covered as “commercial presence” and under a separate investment chapter	No	Yes
Japan – Singapore	Universal *	Positive list approach	Covered as “commercial presence” and under a separate investment chapter	No	No
Japan - Switzerland	Universal*	Negative list approach	Covered as “commercial presence” and under a separate investment chapter	No	Yes
Japan – Thailand	Universal*	Positive list approach	Covered as “commercial presence”	No	No
Korea – Singapore	Universal*	Negative list approach	Separate chapter	Yes	Yes
Malaysia – Pakistan	Universal*	Positive list approach	Covered as “commercial presence” and under a separate investment chapter	No	No
Singapore – Jordan	Universal*	Positive list approach	Covered as “commercial presence”	No	No
Singapore - Panama	Universal*	Negative list approach	Separate chapter	Yes	Yes
Taiwan –	Universal*	Negative list approach	Separate chapter	Yes	Yes

Agreements	Scope/ Coverage	Negotiating modality	Treatment of investment in services	Right of non establishment	Ratchet mechanism
Nicaragua					
ASEAN Framework Agreement on Services	Universal*	Positive list approach	Covered as “commercial presence” and under a separate investment chapter	No	No
ASEAN – Australia – New Zealand	Universal*	Positive list approach	Covered as “commercial presence and under investment	No	No
Australia – New Zealand Closer Economic Relations trade Agreement	Universal*	Negative list approach	Covered as “commercial presence” but no common disciplines on investment	Yes	No
New Zealand - China	Universal*	Positive list approach	Covered as “commercial presence”	No	No
US – Colombia	Universal*	Negative list approach	Separate chapter	Yes	Yes
US – Jordan	Universal*	Positive list approach	Covered as “commercial presence”	No	No
US – Oman	Universal*	Negative list approach	Separate chapter	Yes	Yes
US – Panama	Universal*	Negative list appraoch	Separate chapter	Yes	Yes
US-Singapore	Universal*	Negative list approach	Separate chapter	Yes	Yes
US-Chile	Universal*	Negative list approach	Separate chapter	Yes	Yes

* Air transport and in certain cases cabotage in maritime services is excluded

[1] Honduras, Guatemala and El Salvador

3. Assessing the depth of preferential liberalization in services trade

3.1 Overall trends

The depth of services liberalisation varies considerably across PTAs, with differences notable across sectors, modes of supply, approaches to scheduling commitments (i.e. hybrid vs. negative list approaches) as well as across country groupings (i.e. North-North, North-South and South-South) and partner pairings. While this paper does not attempt a comprehensive assessment of the market opening advances achieved in services-related PTAs across the sample of agreements under review, it draws on a number of important recent contributions to the literature in offering stylized facts about the WTO+ nature of PTAs in services trade.

Sequencing

The sequence of preferential market opening in services rarely, if ever, predates preferential talks in goods trade. Countries that engage in services-related PTAs either pursue such negotiations alongside merchandise trade negotiations in a manner analogous to the WTO's "Single Undertaking" approach or pursue services talks sequentially once a PTA in goods trade has been agreed. The latter approach is more common among South-South PTAs, whereas agreements involving OECD countries typically espouse the Single Undertaking route.

Countries preferring sequential liberalization may wish to test the waters in goods trade first, raising comfort levels with new trading partners. They may also wish to limit the scope for bargaining across several policy areas that comes from WTO-type negotiations, though such a choice may well constrain negotiations given the greater narrowness of the negotiating remit. Sequential liberalization may also allow partners to identify key services inputs and address potential service sector bottlenecks holding back trade in manufactured products or primary commodities. The greater degree of liberalization achieved to date under North-South PTAs, particularly those based on a negative list approach, helps explain why PTAs predicated on a Single Undertaking approach have tended to entail greater levels of market opening.

The fact that PTAs have achieved significant progress in market opening terms when compared to the GATS should come as no surprise when one considers that the WTO commitments under GATS are those brokered in the early 1990's and, in the case of telecommunications and financial services (where most progress was made), in 1997. The vast majority of services-related PTAs were concluded after the entry into force of the GATS. Such agreements have taken advantage both of rising comfort levels afforded by the pedagogical journey undertaken during the Uruguay Round, from the rising level of services-specific trade-related technical assistance dispensed at both the multilateral and PTA levels in the post-Uruguay Round period as well as the far-reaching degree of unilateral liberalization in services markets that characterized the period and which the WTO-GATS has yet been able to catch-up to and consolidate. A more analytically meaningful comparison is thus the one that can be made between the level and nature of PTA commitments and that of negotiating offers made by WTO Members in the ongoing Doha Development Agenda (despite the tactical considerations that

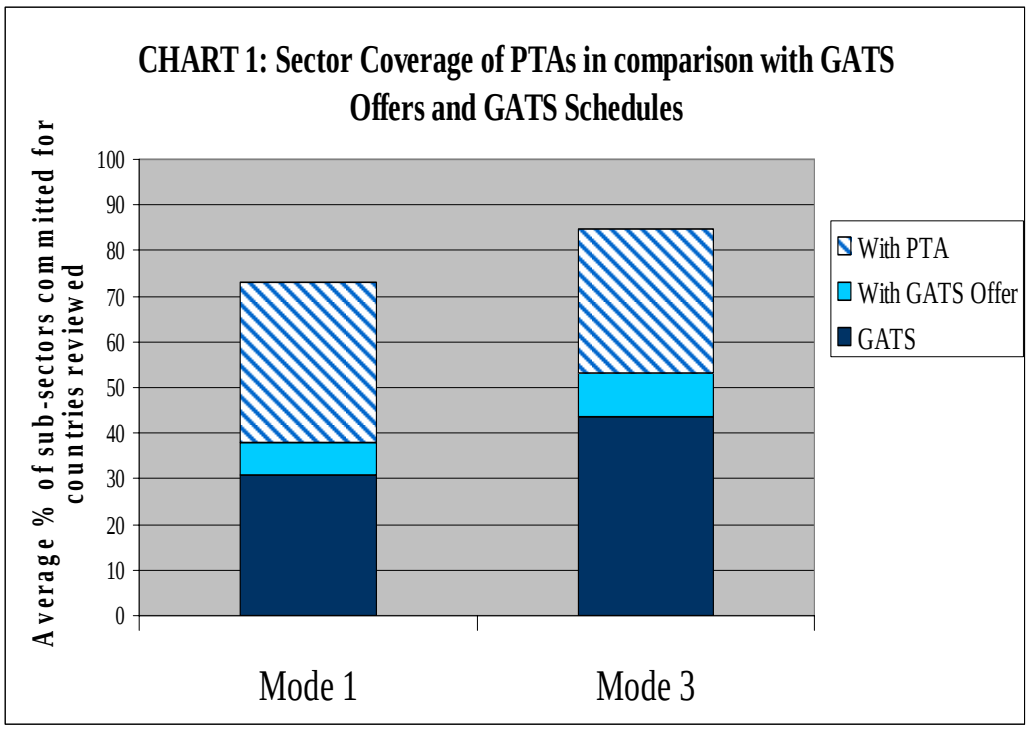
my well hold back services offers in a round that has placed agriculture and NAMA squarely at the centre of discussions).

3.2 How much further than the WTO?

If one can safely assume that the PTAs of today have taken services liberalization further than the situation prevailing at the end of the last round of multilateral negotiations, there are nonetheless marked differences in outcomes that bear noting, Using a sample of 28 PTAs concluded among 29 WTO Members, Roy, Marchetti and Lim (2008) depict differences in the level of commitments scheduled under GATS on Modes 1 (cross-border supply) and 3 (commercial presence), those flowing from GATS offers made (as of January 2008) under the WTO's Doha Development Agenda, as well as under PTAs. The results, summarized in Chart 1 below, offer a measure of the prevailing gap between preferential and multilateral liberalization in services trade across the two leading modes of supplying services. [40]

Chart I shows that the average level of sub-sectors bound in the prevailing GATS schedules is rather low (31% for mode 1 and 44% for mode 3), reflecting the negotiating precaution that characterized the first ever multilateral negotiation in the services field. Chart I further reveals that DDA offers have not modified this landscape in a dramatic fashion (moving up 7 percentage points to 38% for mode 1 and up 9 points to 53% for mode 3 trade). The value-added of PTAs, which is illustrated by the striped part of the bar, is significant. For Mode 1, such coverage reaches 73% on average, almost doubling that achieved by the latest DDA offers. For commercial presence, it reaches 85%, almost doubling the average proportion of sectors covered by existing GATS commitments and still significantly higher what has been offered in the DDA to date.

[40] The PTAs reviewed in the paper are the following: New Zealand-Singapore; EFTA-Mexico; EC-Mexico; Chile-Costa Rica; Japan-Singapore; Singapore-Australia; US-Chile; US-Singapore; Chile-El Salvador; Korea (Rep.)-Chile; EC-Chile; EFTA-Singapore; China-Hong Kong, China; China-Macao, China; EFTA-Chile; US-Australia; Thailand-Australia; Panama-El Salvador; Japan-Mexico; US-Bahrain; US-Oman; US-Central America and Dominica Republic; US-Morocco; US-Peru; Japan-Malaysia; Korea (Rep.)-Singapore; US-Colombia; Singapore-India. This sample includes agreements signed but not yet implemented or notified to the WTO at the time of writing. In computing sector coverage, Roy, Marchetti and Lim looked at the best commitments undertaken by each country across any of its agreements. The EU-15 is counted as one. Macao and Hong Kong's commitments are not computed. In their paper, Roy, Marchetti and Lim focus on Modes 1 and 3, which represent more than 80% of world services trade.



Source: Roy, Marchetti and Lim (2008).

Investigating the WTO+ nature of PTA advances on Mode 3 (commercial presence) – by far the most important means of accessing services markets – the work of Roy, Marchetti and Lim (2008) further reveals significant variance across country groupings. The extent of such variance is shown in Table 4 below. While there is considerable diversity in terms of additional sector coverage in PTAs for individual countries, PTAs are found to go beyond existing GATS commitments and DDA offers across *all* country groupings. The PTA-induced 'jump' in sector coverage for developing countries is much larger than for developed countries, as the latter had higher sectoral coverage levels to start with under their GATS schedules.

Table 4 further highlights sizable differences in Mode 3 liberalization patterns obtaining between agreements pursuing hybrid and negative-list approaches to liberalization, with far greater commitments scheduled under the former. It also shows that PTAs conducted along North-South lines achieve deeper liberalization than those involving South-South partnerships. Such a result is broadly commensurate with the continued dominance of OECD countries in world services trade and investment even as a growing number of developing countries are fast acquiring significant levels of comparative advantage across a wide range of sectors. Such findings may also confirm the superior negotiating leverage that large countries have in preferential confines relative to what is possible at the WTO level.

Table 4: Average Percentage of Sub-Sectors Subject toMarket Access Commitments on Mode 3, Selected Country Groupings

	GATS	With GATS DDA offer	With PTA	Δ vs best WTO treatment
ALL	44%	53%	85%	32%
Developing Countries	36%	46%	86%	40%
Developed Countries	67%	74%	82%	8%
Hybrid Listing	57%	66%	69%	3%
Negative Listing	37%	47%	93%	46%
US PTA partner	30%	39%	93%	54%
Not US PTA Partner	56%	66%	76%	10%

Source: Roy, Marchetti and Lim (2008); amended by authors

Several PTAs, particularly (but not only) those negotiated along South-South lines, show a tendency to only marginally deepen liberalisation commitments beyond the GATS. This raises serious questions about their very rationale, all the more so when signatories resort to the GATS framework for rule-making purposes without attempting to craft new or PTA-specific rules to govern services trade and investment among them.[41]

One factor that clearly influences the level of commitments undertaken in services-related PTAs is the economic importance of the trading partners involved. Roy, Marchetti and Lim (2008) and Marchetti and Roy (2008) show how the United States invariably secures greater commitments from its trading partners than the commitments such countries are willing to undertake in PTAs with other trading partners (including other OECD country partners). Marchetti and Roy (2008) argue that such a finding can be traced to a mix of political influence and foreign policy factors, and the relative importance of the US market for its trading partners' key goods exports (such

[41] Such a sample would include, for instance, EFTA countries, India, the European Communities (prior to the EPA with CARIFORUM and, to some extent, the EU-Chile FTA), or the ASEAN countries (other than Singapore). In some particular cases, these more limited advances may be due to the fact that PTA negotiations took place before the last DDA offer, such that what was conceded in the PTA may later find its way into a revised GATS offer.

as in the case of the Central American countries, the Dominican Republic or the Andean countries).

Sectoral and modal patterns

Turning to sectoral patterns of liberalization, the available empirical evidence attests to significant WTO+ advances across the full range of traded services. Using an index that ranks scheduled commirments using a scale from 1 to 100, Marchetti and Roy (2008) show how PTAs have registered far-reaching advances in comparison to GATS commitments and DDA offers across all sectors (see Table 5 below). This includes both sectors that have attracted less commitments and DDA offers under the GATS - for example audiovisual services - as well as those that have generally proven more attractive in a multilateral setting, such computer, tourism or telecom services.

Table 5. Comparing GATS Commitments, GATS DDA Offers, and 'Best' PTAs Commitments Across All Members Reviewed, per Selected Sector Grouping

SECTORS	GATS	GATS DDA OFFERS	PTAs
Professional	30	39	67
Computer	55	74	93
Postal-Courier	14	20	53
Telecom	51	58	80
Audiovisual	17	20	50
Construction	40	46	75
Distribution	32	41	76
Education	18	25	57
Environmental	20	30	62
Financial	36	40	53
Health	8	11	34
Tourism	51	61	83
Maritime	12	23	57
Rail	14	20	52
Road	16	18	56
Auxiliary Transport	21	24	58

Note: Scores for Modes 1 and 3 are combined. Scale of 1 to 100. On the basis of best (most liberalizing) PTA commitments.
Source: Marchetti and Roy (2008).

With the notable exception of land transportation issues, where physical proximity stands out as a determinative trade facilitating feature driving the cross-border liberalization process, PTAs continue to encounter resistance in opening up those service sectors that have proven difficult to address at the multilateral level. Most PTAs thus tend to exclude the bulk of air transportation services (with the notable exception of the EU for intra-EU traffic) from their coverage as well as a broad swath of public services.

Relatively limited progress – though still WTO+ in most areas - has similarly been achieved in PTAs in sectors where particular policy sensitivities arise, such as maritime transport and audio-visual services, energy services and to some extent (though more so for some countries than others) on the movement of service suppliers. Other sectors that generally fit this overall pattern include postal and courier services (though not express delivery), health and education services.

A contrario, PTAs have proven useful settings in which to advance liberalization prospects in market segments characterized by rapid technological and commercial change. The area of e-commerce or so-called "digital trade", encompassing a broad range of business and IT-related services, which was not yet a commercial reality at the time of the Uruguay Round, is one prominent example (See Box 3 below).

Box 3. PTAs and Digital trade

PTAs increasingly reflect the growing electronic cross-border delivery of services and digital products (e.g. software) by incorporating trade rules for e-commerce.
What started with the incorporation of a non-binding E-commerce Chapter in the US-Jordan PTA in 2000subseuently led to the conclusion of the first legally binding US E-commerce Chapter in bilateral trade agreements in the US-Singapore FTA of 2003 and to a further flurry of US-led bilateral PTAs incorporating E-commerce Chapters that are subject to dispute settlement provisions. But the trend has spread further with PTAs such as Singapore-Australia, Thailand-Australia, India-Singapore, and other containing digital trade rules . Other PTAs (Maghreb Arab Union state, India-Thailand, Japan-Mexico, Japan-Asean, India-ASEAN, China-ASEAN, etc.) and trade-related statements from APEC and cooperation agreements also increasingly contain binding and non-binding pledges related to ICTs and e-commerce. The PTAs are thus functioning as a laboratory for digital trade rules with a demonstration effect which is potentially useful for future multilateral or other preferential trade negotiations.

E-commerce Chapters with a focus on digital products

E-commerce chapters of PTAs following the "US template" formalize a definition of digital content products, confirm the applicability of WTO trade rules to e-commerce, the applicability of provisions on cross-border trade in services apply to electronically supplied services, assure a clear zero-duty rate on the content of digital trade and provide for non-discrimination and MFN treatment for digital products such as music, films, software (Table 1). Interestingly from the point of view of rules of origin, in this template digital products must not be fully created and exported via one of the contracting parties of the respective PTA to benefit from non-discrimination or MFN.

Cross-Border Trade in Services Chapters geared towards electronic trade

The Cross-Border Trade in Services Chapters of newly agreed US-led PTAs also innovate to the benefit of the digital delivery of services. The PTAs use a negative list approach to schedule service trade commitments. Assuming that no reservations are made, this top-down approach guarantees that narrow or outdated classification schemes and uncertainties relating to the mode of delivery do not limit the applicability of commitments to digitally-delivered

services. Importantly the PTAs specify that '*[n]either Party may require a service supplier of the other Party to establish or maintain a representative office or any form of enterprise, or to be resident, in its territory as a condition for the cross-border supply of a service*.". MFN exemptions are not possible. Again the devil is in the detail as attention must be paid to specified non-conforming measures (e.g. in the case of US-led PTAs US state level regulation are sometimes listed as exception). On the side of services rules, the PTAs introduce strengthened transparency requirements, sector-specific mutual recognition annexes (for example for professional services) and binding rules on domestic regulation useful for digital trade.

"Deep" digital trade rules

Two other developments in PTAs foster digital trade rules:

Non-binding Joint Understandings on e-commerce calling for liberal digital trade principles and rules fostering the diffusion of ICTs and e-commerce. A number of PTAs spell out a cooperation agenda on various aspects of the information society but in particular in areas such as: telecommunications policy, ICT standards / conformity assessments, interconnection / interoperability issues, cyber-security, electronic signatures, the balance between privacy protection and the free cross-border flow of information, intellectual property rights, consumer confidence in e-commerce, etc.

Incorporation of 'deep integration' digital trade principles as an integral component of bilateral trade agreements and sometimes also subject to the dispute settlement provisions. Such 'deep' digital trade provisions can be found relating to the following topics: domestic regulation, transparency, consumer protection, data protection, authentication and digital signatures, and paperless trading .

Source: Wunsch-Vincent (2008).

Market-opening advances are also notable in sectors where new, post-Uruguay Round, pro-liberalization constituencies have emerged seeking to use trade agreements to secure expanded opportunities in world markets. This is notably the case of express delivery services, which feature prominently in a number of recent PTAs. Similarly, new areas of financial services, such as asset management or financial services delivered through electronic means; trade in some segments of higher education and related services (e.g. vocational training and educational testing); as well as the wellness industry situated at the interface of tourism and health services, are all receiving greater attention in many recent preferential agreements, including those brokered along South-South lines.

In some cases, market opening advances rest on a complementary set of new disciplines. Such a trend is most visible in the field of investment, where PTAs have achieved significant forward movement over the WTO. It is also notable in the area of procurement liberalization. A further example of the close nexus between market opening and novel (pro-competitive) rule-making can be found in the tourism sector, where the EU-CARIFORUM Economic Partnership Agreement recently blazed a new trail (see Box 4). It is possible that many such advances could be replicated at the WTO level in the Doha Round or beyond, all the more so as most of them are actively being discussed in ongoing negotiations under the GATS and have been the object of collective requests advanced by various coalitions of like-minded WTO Members.

Box 4. Tourism liberalization in the CARIFORUM-EU EPA

The tourism sector stands out as one in which developing countries possess clear comparative advantages in services trade. Accordingly, several developing country governments have for some time been clamoring for provisions in trade agreements dedicated to the sector and its specificities. Such calls led to the formulation of a draft GATS Annex on tourism services during the course of the Doha Round and to the formulation of a collective request sponsored by a majority of developing country members of the WTO, several of which from the Caribbean region. The collective inability of WTO Members to complete the Doha Round has so far stymied progress in this area. Not surprisingly, proponents of tourism trade liberalization took their case to subsidiary settings.

The CARIFORUM-EU Economic Partnership Agreement concluded in 2008 offered a natural setting for testing out several of the ideas advanced in the submissions described above and to seek to advance negotiations in a sector of clear offensive interest to the developing country partner. PTA advances in this case offer the interesting example of reverse engineering by adapting proposals or draft rules initially targeted at the WTO level. The precedent set in the EPA is likely to inform the treatment of tourism in other PTAs involving developing countries as well as at the WTO level, be it in the Doha Development Agenda or beyond.

Initially, CARIFORUM Members had proposed the inclusion of a distinct tourism annex in the EPA. The origins of this seems to have been the WTO Doha Round proposal submitted by Bolivia, the Dominican Republic, Ecuador, El Salvador, Honduras, Nicaragua, Panama, Peru and Venezuela in 2001.[42] The latter proposal was the inspiration for the draft text on tourism which was formulated by the Caribbean Hotel and Tourism Association and adopted by the Caribbean Regional Negotiation Machinery in the EPA context.

(i) Mutual recognition

On the question of the negotiation of a mutual recognition agreement (MRA) for tourism service providers, the EPA provides that "*the Parties shall co-operate towards the mutual recognition of requirements, qualifications, licenses or other regulations in accordance with Article 85*…."[43] Article 85, which deals with mutual recognition more generally, reaffirms the Parties' right to require that natural persons possess the necessary qualifications and/or professional experience to supply covered services; commits the Parties to encourage the relevant professional bodies in their respective territories to jointly develop and provide recommendations on mutual recognition to the CARIFORUM-EC Trade and Development Committee to determine the criteria to be applied by the Parties for the authorization, licensing, operation and certification of investors and services suppliers. Tourism is identified as one of the priority sectors for the development of

[42] World Trade Organization, "Communication by Bolivia, Dominican Republic, Ecuador, El Salvador, Honduras, Nicaragua, Panama, Peru and Venezuela: Draft Annex on Tourism," S/CSS/W/107, September 26, 2001.

[43] EC-CARIFORUM EPA, Article 114.

mutual recognition arrangements under the Agreement.[44] The EPA specifically mandates the EC and CARIFORUM to encouraging (i.e. a hortatory, or "best endeavors" commitment) their relevant professional bodies in their respective territories to start negotiations three years after the EPA's entry into force in order to jointly develop and provide recommendations on mutual recognition.

(ii) Competition policy disciplines

One important element of the Doha Development Agenda proposal which the Caribbean Hotel and Tourism Association maintained in its EPA draft was the creation of a competitive safeguard for tourism.[45] The inclusion of disciplines on anti-competitive practices was of key importance to CARIFORUM states as the global tourism industry is characterized by vertically integrated market structures and consolidated distribution channels controlled by a limited number of large international players,[46] many of which are based in the EU. Specifically, in accordance with Chapter 1 of Title IV dealing with competition policy, Article 111 EPA compels the parties to maintain or introduce measures to prevent suppliers from materially affecting 'the terms of participation in the relevant market for tourism services by engaging in or continuing anti-competitive practices, including, *inter alia*, abuse of dominant position through imposition of unfair prices, exclusivity clauses, refusal to deal, tied sales, quantity restrictions or vertical integration.' The EPA provision on the prevention of anti-competitive practices is legally binding.[47]

(iii) Trade-related capacity building

Also notable in the EPA's treatment of tourism services is the fact that the sector features distinct development co-operation provisions, in contrast to other sectors where such issues are addressed in a generic manner. The EPA puts forward an explicit commitment on the part of the EC to help in the advancement of the tourism sector in the CARIFORUM states and sets out a non-exhaustive list of specific areas in which the Parties agree to co-operate. This includes capacity building for environmental management, the development of internet-based marketing strategies for small and medium sized tourism enterprises, as well as the upgrading of national accounts systems with a view to facilitating the introduction of tourism satellite accounts[48] at the regional and local level.

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[44] EC-CARIFORUM EPA, Article 85 (3).

[45] Incidentally, it is worthy of note that the EC's reaction to Dominican Republic's Doha Development Agenda proposal was to support the main intentions of the proposal, while not explicitly endorsing the Tourism Annex to the GATS. However, the EC signaled that two issues in the draft- tourism and sustainable development and competitive safeguards- merited further consideration. See Dunlop, "Tourism Services Negotiations Issues," 10.

[46] CRNM, "The Treatment of Tourism in the CARFORUM-EC Economic Partnership Agreement," 2.

[47] By contrast, the other provisions in the Section 7, which addresses the tourism sector, are non-binging. For a fuller discussion of the treatment of tourism under the EPA, see Sauvé and Ward (2009), The EC-CARIFORUM Partnership Agreement: Assessing the Outcome on Services and Investment." *ECIPE Discussion Paper.* Brussels: European Centre for International Political Economy. Available at: http://www.ecipe.org/publications/ecipe-working-papers/the-ec-cariform-economic-partnership-agreement-assessing-the-outcome-on-services-and-investment.

[48] A Tourism Satellite Account (TSA) is a statistical instrument to analyse the economic importance of tourism. According to the European Commission, 'a complete TSA contains detailed production accounts of the tourism industry and their linkages to other industries,

Sources: Sauvé and Ward (2009, 2009a).

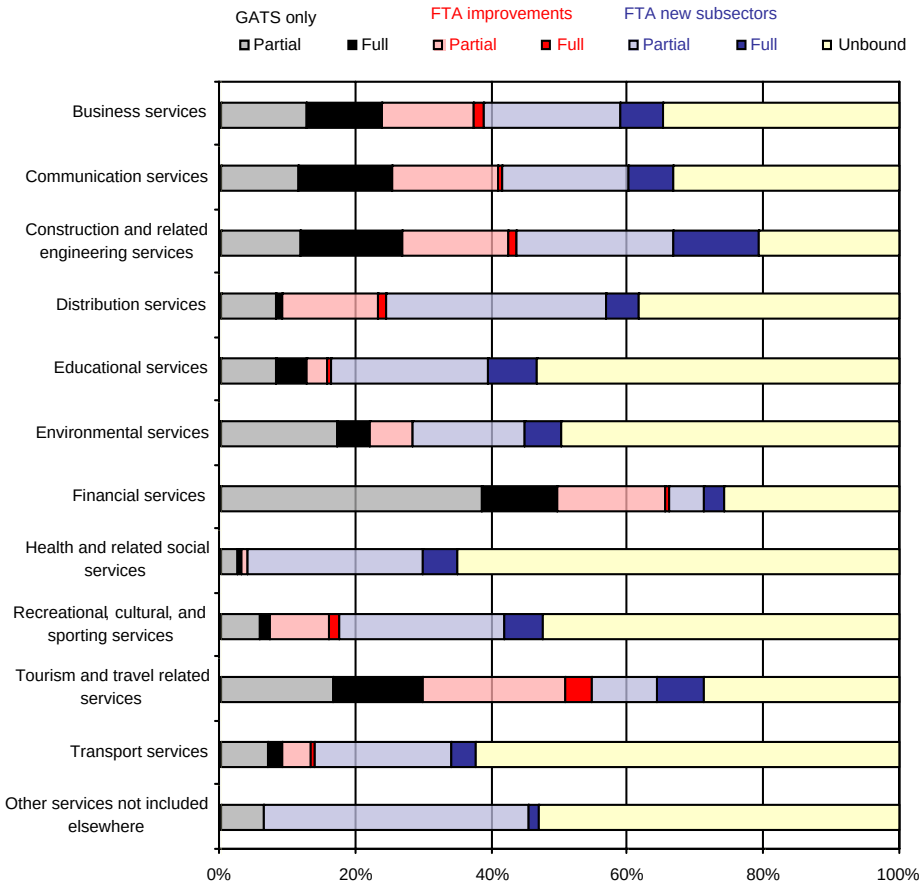
The sectoral patterns of PTA-induced market opening in services trade described above appear to hold at the regional level. This is evidenced for instance in the work of Fink and Molinuevo (2007), which offers an aggregated measure of the GATS+ nature of market opening commitments in a sample of service-related PTAs concluded among Asian countries (see Charts 2 below for a depiction of sectoral advances). Such findings reveal that while GATS+ advances are significant across all sectors, they are particularly noticeable in the areas of business services (reflecting the emergence of digital trade, e-commerce and the outsourcing revolution in services); distribution; education, health and transport services, all areas that have proven difficult in the WTO context during the Uruguay Round and in the more recent context of the Doha Development Agenda.

Meanwhile, the lesser relative progress registered in areas such as telecommunications and financial services in the South-East Asian context recalls that these are precisely the sectors where GATS negotiations have to date been most successful. This may well lessen the scope or perceived need for significant new advances in a PTA context. This is so even as both sectors are ones in which PTAs, in Asia and beyond, have continued to reap market opening advances relative to conditions prevailing at the end of 1997 when both the Agreement on Basic Telecommunications and the Financial Services Agreement were completed in a GATS setting.

Using the Fink-Molinuevo methodology and applying it to the four largest members of CARIFORUM in the context of the EU-EPA, Sauvé and Ward (2009) reveal a broad pattern of WTO+ or WTO-X advances arising at the preferential level (see Annex Charts 1 to 4).

employment, capital formation and additional non-monetary information on tourism. See online at http://www.unwto.org/statistics/index.htm and http://ec.europa.eu/enterprise/services/tourism/tourism_satellite_account.htm.

Chart 2. GATS+ advances in East Asian PTAs: sectoral breakdown

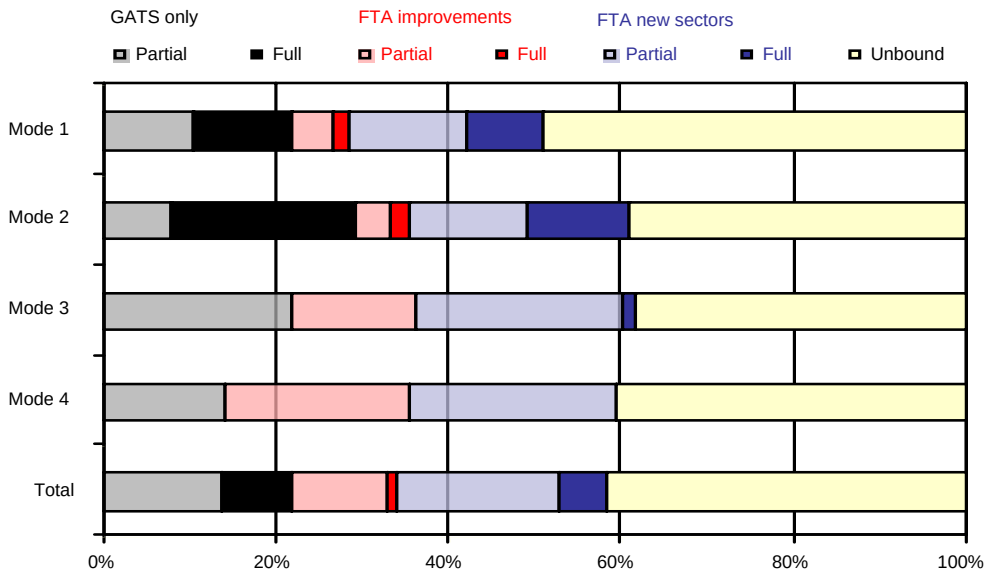


Source: Fink and Molinuevo (2007).

The East Asian PTA experience depicted in Fink and Molinuevo (2007) confirms the partial, incremental, nature of market opening in services trade. Such an observation is particularly apparent when commitments are analysed on a modal basis (see Chart 3 below). From a positive (albeit not entirely surprising point of view given the reluctance of countries to contemplate Mode 4 liberalization on an MFN basis in the WTO), the most significant sources of GATS+ advances in East Asian PTAs relate to the two modes of supply likely to generate the strongest developmental returns: mode 4 (movement of natural persons) – the least committed of all modes under GATS – and mode 3 (commercial presence) – the most committed of all modes subject to GATS bindings and the principal means through which services are traded internationally.[49]

[49] One example drawn from the Asian experience relates to the labour mobility provisions found in recent Japanese PTAs, which feature novel provisions aimed at assisting partner countries with training in the home country prior to their admission as professionals in the Japanese labour market with a view to complying with Japanese licensing requirements in nursing and other health-related occupations. While the numerical quotas agreed by Japan in these areas remain low relative to the supply capacity (and negotiating interests) of sending countries, such provisions nonetheless represent a step forward in the treatment of Mode 4 issues in a context of population ageing and labour market shortages in OECD countries.

Chart 3. GATS+ advances in East Asian PTAs : modal breakdown



Source: Fink and Molinuevo (2007).

As obtains in other preferential settings and at the WTO level, the East Asian PTA experience reveals lesser preferential advances in regard to Modes 1 (cross-border supply) relative to Mode 3 (commercial presence).This reflects the generally greater precaution shown towards transactions which many host countries feel they cannot (or cannot easily) regulate.

Evidence of iterative learning by doing

The relationship between PTAs and the WTO is not unidirectional in character but involves iterative, two-way, interaction between the two layers of trade governance in ways that can inform, subsequent patterns of rule-making and market opening at both the PTA and WTO levels. Examples of such interaction can notably be found in areas where WTO jurisprudence has clarified or interpreted the scope of key provisions governing services trade that are typically found both in the WTO-GATS and in the services and investment chapters of PTAs. Baptisto (2009), for instance, has found evidence of NFATA-minus treatment of recreational services in the reservation lists of the United States following the decision of the WTO's Dispute Settlement and Appellate (DSB and AB) bodies in the area of online gambling (United States-Gambling Services). Similarly, the most recent DSB and AB decisions in the China - Publications and Audiovisual Products dispute has already prompted some observers to note the need for China to adjust its future PTA commitments with a view to ensuring the preservation of adequate policy space with which to pursue cultural policy objectives (Shi and Chen, forthcoming).

The co-existence of hard and soft law provisions

A final, salient, trend emerging from the most recent generation of PTAs that has both a rule-making and market opening dimension concerns the increasing reliance that is made, particularly in agreements brokered by the EC, on a set of non-binding provisions embedded in PTAs alongside treaty provisions that are legally binding and enforceable.

Advances of this type reflect the ever-broadening remit of trade rule-making and the commensurate desire of Parties to assign to regulatory cooperation a number of trade- and investment- facilitating roles. For various reasons, such PTA advances may well be limited to preferential settings and encounter difficulties in 'migrating' to the WTO. This may notably the case where Parties harbour concerns over MFN-induced free riding, where particular policy sensitivities arise at the WTO level that can nonetheless be contained or addressed in a PTA setting, or where Parties may simply not deem binding and enforceable obligations a desirable outcome. The area of cultural cooperation (see Box 5) would appear to correspond to the former category of policy domains while that of aid for trade and its design in the services field likely falls more squarely within the latter category (see Box 6).

Box 5. Cultural cooperation in the EU-CARIFORUM EPA

A novel feature of the CARIFORUM EPA is its inclusion of a Protocol on Cultural Co-operation between the Parties. The Protocol establishes a clear precedent in addressing matters relating to cultural industries within PTAs, laying the basis for the inclusion of similar provisions in other EPAs. The inclusion of language on cultural cooperation matters marks a significant evolution in EU attitudes towards the subject matter in a trade policy context, hitherto marked by a desire to preserve maximum policy autonomy by eschewing any commitments in trade agreements and, in the case of the DDA, by refusing to direct negotiating requests to its trading partners and to entertain offers in response to trading partner requests in cultural industries. The advances made in the Protocol respond to CARIFORUM members' strong offensive interests in this area, notably the music industry.

The EPA Protocol establishes a framework within which the Parties can co-operate with a view to facilitating exchanges of cultural activities, goods and services, the movement of artists and other cultural professionals and to

improving cinematographic cooperation between the Parties The protocol can be viewed as the first concrete response to Article 16 of the UNESCO Convention on the Protection and Promotion of the Diversity of Cultural Expressions dealing with preferential treatment. According to CARIFORUM officials, the conclusion of co-production agreements, which the protocol calls for, will make it possible for Caribbean audiovisual producers to access new sources of funding for creative projects. Given the EC's longstanding sensitivities in the audio-visual sector, the Protocol likely represents as close to new market access opportunities as the EC's EPA partners could have hoped for without actually resulting in new liberalization commitments on national treatment or market access.
Source: Sauvé and Ward (2009)

Box 6. Aid for Trade in Services: Co-operation & Financing for Development in the EU-CARIFORUM EPA

The co-operation elements of the EU-CARIFORUM EPA respond to the aim of EU Members to infuse the Agreement with a concrete development dimension. In so doing, the EPA charts useful new territory at a time when the multilateral community is struggling to give operational meaning to the concept of Aid for Trade.
The EPA text does not feature explicit language on the level of development financing made available overall nor does it spell out the specific issues and sectors subject to the Agreement's coverage. This has sparked much criticism throughout the CARIFORUM region over the alleged unbalanced nature of the Agreement insofar as its development provisions remain somewhat abstract and not legally enforceable while its liberalization commitments are up-front, legally binding and enforceable. Responding to such critiques, the Caribbean Regional Negotiating Machinery (CRNM), which led the negotiations on the CARIFORUM side, cautioned that "any perceptions about the EPA's practical deficiencies with respect to the treatment of development and development cooperation and assistance should first be tempered by the recognition that as a trade agreement, the EPA should not be perceived to be the primary vehicle through which development may be achieved."[50] Rather, it should be considered as "one strategic instrument in a range of economic development strategies."[51]
According to the Joint Declaration on Development Co-operation, which is annexed to the EPA and constitutes an integral part of it, a package of €165 million has been set aside for the six years following the Agreement's entry into force to fund activities identified and rank-ordered in the Caribbean's regional indicative plan (RIP).
In addition to funding for the regional indicative plan, each CARIFORUM state will receive funds for its national indicative plans (NIP) but must identify two priority projects for such additional funding. The Dominican Republic and

[50] CRNM, 'RNM Update 0802', electronic newsletter, available online at http://www.crnm.org/documents/updates_2008/rnmupdate0802.htm., accessed 19 April 2008.
[51] Ibid.

Jamaica announced that they would be using some of the financing under their respective NIPs for purposes of EPA implementation.
The minimum cost of implementing the EPAs provisions on Investment, Trade in Services and E-Commerce and addressing the capacity constraints at the national and regional levels has been estimated at €15.6 million.[52] Key areas concerned include the building of regulatory capacity, overcoming information asymmetries in order to assist CARIFORUM firms and entities to identify business opportunities in the European market and the development of productive capacity in goods and cultural services.
Specific technical assistance efforts are to be directed at the following objectives: (i) improving the ability of CARIFORUM service suppliers to gather information on and meet regulations and standards of the EC Parties; (ii) improving the export capacity of local service suppliers; (iii) facilitating interaction and dialogue between service suppliers of both Parties; (iv) addressing quality and standards in needs in those areas where the CARIFORUM states have undertaken commitments; (v) developing and implementing regulatory regimes for specific services at the CARIFORUM level and in the signatory CARIFORUM states; (vi) establishing mechanisms for promoting investment and joint ventures between service suppliers of the Parties; and (vii) enhancing the capacities of investment promotion agencies in CARIFORUM states.[53]
Source: Sauvé and Ward (2009).

[52] CARICOM Secretariat, "Implementation of the CARIFORUM-EC Economic Partnership Agreement." (Georgetown: CARICOM Secretariat, 2008), 10. The constraints identified include insufficient numbers of specialists and experts; limited human resources, both within the public and private sectors; the absence of an organized Services sector body through which the stakeholders can be mobilized; general absence of infrastructure; and the inadequacy of financial resources.

[53] Ibid., Article 121 (2).

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ANNEX

TABLE 1. LIST OF PREFERENTIAL TRADE AGREEMENTS (PTAS) THAT INCLUDE PROVISIONS ON TRADE IN SERVICES

Number	Agreement	Type
1	ASEAN - China (S)	EIA
2	Australia - New Zealand (ANZCERTA) (S)	EIA
3	CARICOM (S)	EIA
4	EFTA (S)	EIA
5	MERCOSUR (S)	EIA
6	Australia – Chile	FTA & EIA
7	Brunei Darussalam – Japan	FTA & EIA
8	Canada – Chile	FTA & EIA
9	Canada – Peru	FTA & EIA
10	Chile – Colombia	FTA & EIA
11	Chile - Costa Rica (Chile - Central America)	FTA & EIA
12	Chile - El Salvador (Chile - Central America)	FTA & EIA
13	Chile – Japan	FTA & EIA
14	Chile – Mexico	FTA & EIA
15	China - Hong Kong, China	FTA & EIA
16	China - Macao, China	FTA & EIA
17	China - New Zealand	FTA & EIA
18	China – Singapore	FTA & EIA
19	Costa Rica – Mexico	FTA & EIA
20	Dominican Republic - Central America - United States Free Trade Agreement (CAFTA-DR)	FTA & EIA
21	EC – Albania	FTA & EIA
22	EC - CARIFORUM States EPA	FTA & EIA
23	EC – Chile	FTA & EIA
24	EC – Croatia	FTA & EIA
25	EC - Former Yugoslav Republic of Macedonia	FTA & EIA
26	EC – Mexico	FTA & EIA
27	EFTA – Chile	FTA & EIA
28	EFTA - Korea, Republic of	FTA & EIA
29	EFTA – Mexico	FTA & EIA
30	EFTA – Singapore	FTA & EIA
31	European Economic Area (EEA)	EIA
32	Iceland - Faroe Islands	FTA & EIA
33	India – Singapore	FTA & EIA
34	Japan - Indonesia	FTA & EIA
35	Japan – Malaysia	FTA & EIA

36	Japan – Mexico	FTA & EIA
37	Japan – Philippines	FTA & EIA
38	Japan – Singapore	FTA & EIA
39	Japan - Switzerland	FTA & EIA
40	Japan – Thailand	FTA & EIA
41	Japan - Viet Nam	FTA & EIA
42	Jordan – Singapore	FTA & EIA
43	Korea, Republic of – Chile	FTA & EIA
44	Korea, Republic of – Singapore	FTA & EIA
45	Mexico - El Salvador (Mexico - Northern Triangle)	FTA & EIA
46	Mexico - Guatemala (Mexico - Northern Triangle)	FTA & EIA
47	Mexico - Honduras (Mexico - Northern Triangle)	FTA & EIA
48	Mexico – Nicaragua	FTA & EIA
49	New Zealand – Singapore	FTA & EIA
50	Nicaragua - Chinese Taipei	FTA & EIA
51	North American Free Trade Agreement (NAFTA)	FTA & EIA
52	Pakistan – Malaysia	FTA & EIA
53	Panama – Chile	FTA & EIA
54	Panama - Costa Rica (Panama - Central America)	FTA & EIA
55	Panama - El Salvador (Panama - Central America)	FTA & EIA
56	Panama - Honduras (Panama - Central America)	FTA & EIA
57	Panama – Singapore	FTA & EIA
58	Panama and Chinese Taipei	FTA & EIA
59	Peru – China	FTA & EIA
60	Peru – Singapore	FTA & EIA
61	Singapore – Australia	FTA & EIA
62	Thailand – Australia	FTA & EIA
63	Thailand - New Zealand	FTA & EIA
64	Trans-Pacific Strategic Economic Partnership	FTA & EIA
65	US – Australia	FTA & EIA
66	US – Bahrain	FTA & EIA
67	US – Chile	FTA & EIA
68	US - Jordan	FTA & EIA
69	US – Morocco	FTA & EIA
70	US - Oman	FTA & EIA
71	US - Peru	FTA & EIA
72	US - Singapore	FTA & EIA
73	EC (15) Enlargement	CU & EIA
74	EC (25) Enlargement	CU & EIA
75	EC (27) Enlargement	CU & EIA
76	EC Treaty	CU & EIA
Total number of services PTAs		76
Total number of services only PTAs		6

Total number of goods PTAs	196
Total number of PTAs in force	272
Total number of services PTAs as a percentage of total RTAs in force	27.94%

Source: World Trade Organisation, RTAs Database. Available online from http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx .
Note:
WTO statistics on PTAs are based on notification requirements rather than on physical numbers of PTAs. Thus, for an PTA that includes both goods and services, two notifications are counted (one for goods and the other services), even though it is physically one PTA.

TABLE 2. LIST OF 'SERVICES ONLY' PTAS

Number	Agreement	Type
1	ASEAN - China	EIA
2	Australia - New Zealand (ANZCERTA)	EIA
3	CARICOM	EIA
4	EFTA	EIA
5	MERCOSUR	EIA
6	European Economic Area (EEA)	EIA

Source: World Trade Organisation, RTAs Database. Available online from http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx .
Note: In the WTO's RTA Database, these agreements are listed as covering services only.

TABLE 3. CLASSIFICATION OF PREFERENTIAL TRADE AGREEMENTS (PTAS) FEATURING SERVICES PROVISIONS BY COUNTRY GROUPINGS (NORTH-NORTH, NORTH-SOUTH, SOUTH-SOUTH)[54]

Number	N-N	N-S	S-S
1	Australia - New Zealand (ANZCERTA)	Australia - Chile	ASEAN - China
2	EFTA	Brunei Darussalam - Japan	CARICOM
3	European Economic Area (EEA)	Canada - Chile	MERCOSUR
4	EC (15) Enlargement	Canada - Peru	Chile - Colombia
5	EC (25) Enlargement	Chile - Japan	Chile - Costa Rica (Chile - Central America)
6	EC (27) Enlargement	China - New Zealand	Chile - El Salvador (Chile - Central America)
7	EC Treaty	Dominican Republic - Central America - United States Free Trade Agreement (CAFTA-DR)	Chile - Mexico
8	Iceland - Faroe Islands	EC - Albania	China - Hong Kong, China
9	Japan - Switzerland	EC - CARIFORUM States EPA	China - Macao, China
10	US – Australia	EC - Chile	China – Singapore

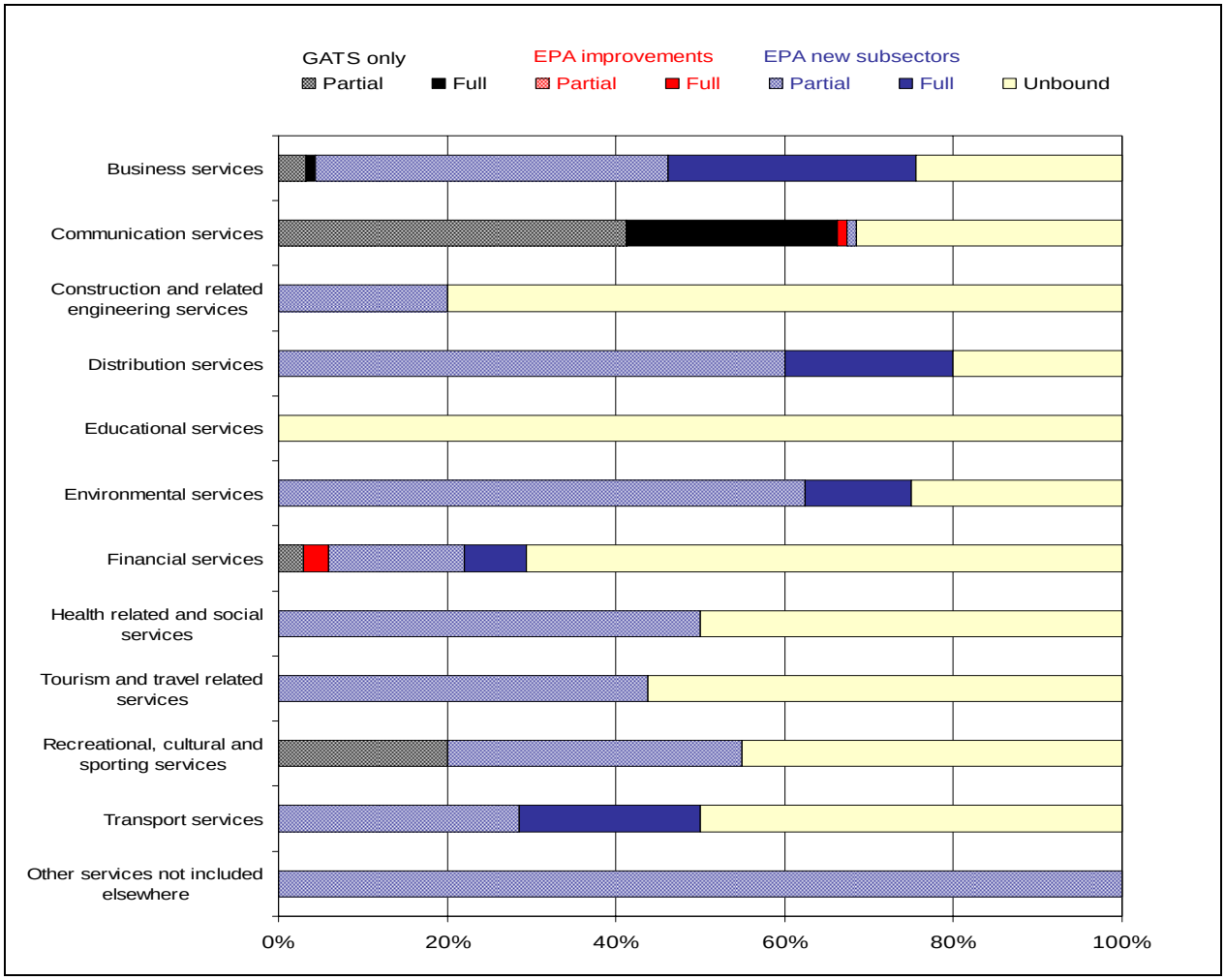
[54] The term "PTAs" subsumes all categories of preferential agreements (i.e. customs unions, free trade agreements and economic unions).

11	EC - Croatia	Costa Rica - Mexico
12	EC - Former Yugoslav Republic of Macedonia	India – Singapore
13	EC - Mexico	Jordan - Singapore
14	EFTA - Chile	Korea, Republic of - Chile
15	EFTA - Korea, Republic of	Korea, Republic of – Singapore
16	EFTA - Mexico	Mexico - El Salvador (Mexico - Northern Triangle)
17	EFTA - Singapore	Mexico - Guatemala (Mexico - Northern Triangle)
18	Japan - Indonesia	Mexico - Honduras (Mexico - Northern Triangle)
19	Japan - Malaysia	Mexico - Nicaragua
20	Japan - Mexico	Nicaragua – Chinese Taipei
21	Japan - Philippines	Pakistan – Malaysia
22	Japan - Singapore	Panama – Chile
23	Japan - Thailand	Panama - Costa Rica (Panama - Central America)
24	Japan - Viet Nam	Panama - El Salvador (Panama - Central America)
25	New Zealand - Singapore	Panama - Honduras (Panama - Central America)
26	North American Free Trade Agreement (NAFTA)	Panama - Singapore
27	Singapore - Australia	Panama and Chinese Taipei
28	Thailand - Australia	Peru - China
29	Thailand - New Zealand	Peru - Singapore
30	Trans-Pacific Strategic Economic Partnership	
31	US – Bahrain	
32	US – Chile	
33	US - Jordan	
34	US – Morocco	
35	US – Oman	

36	US – Peru
37	US - Singapore

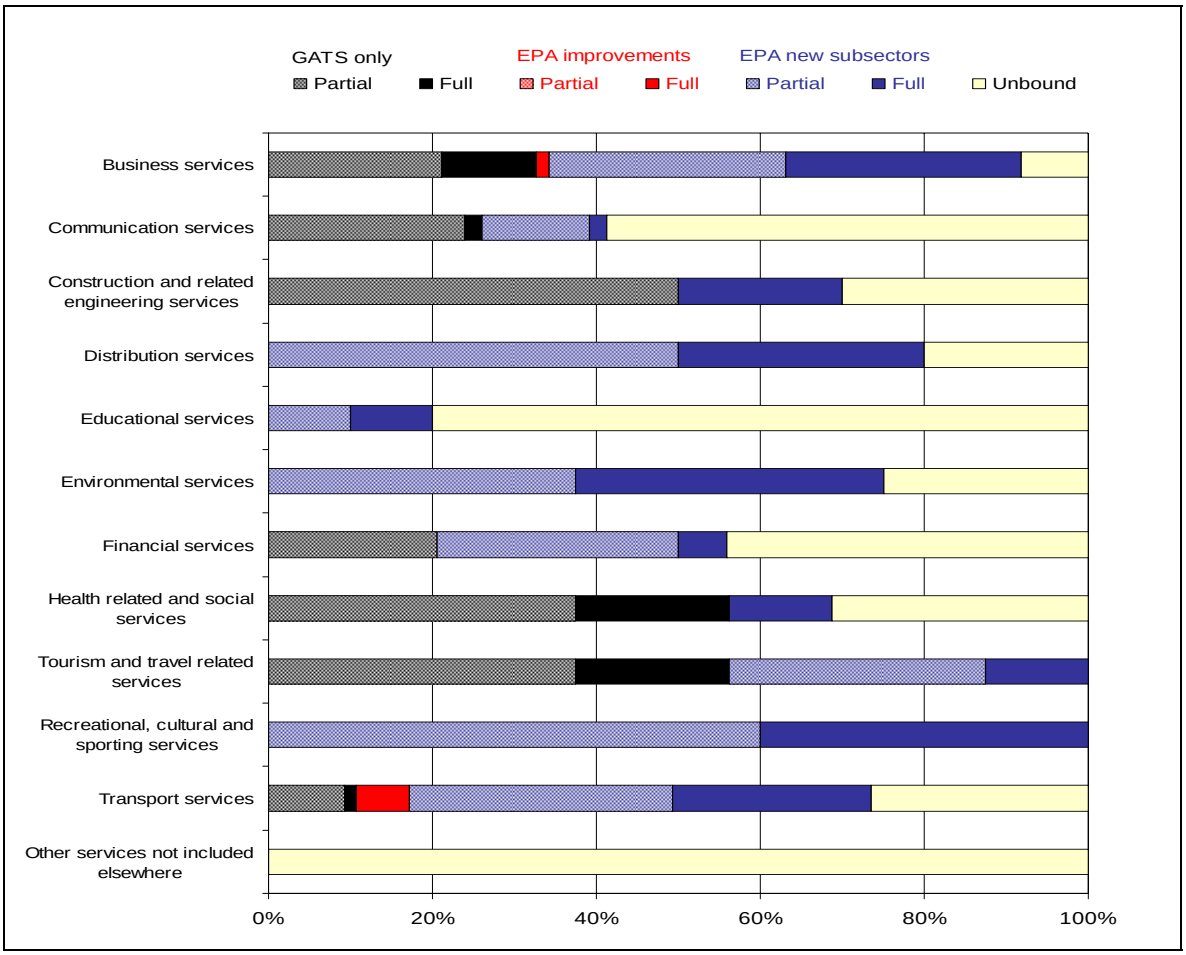
Source: World Trade Organisation, RTAs Database. Available online from http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx .

Chart 1. Comparing the GATS and EU-CARIFORUM Commitments: Barbados



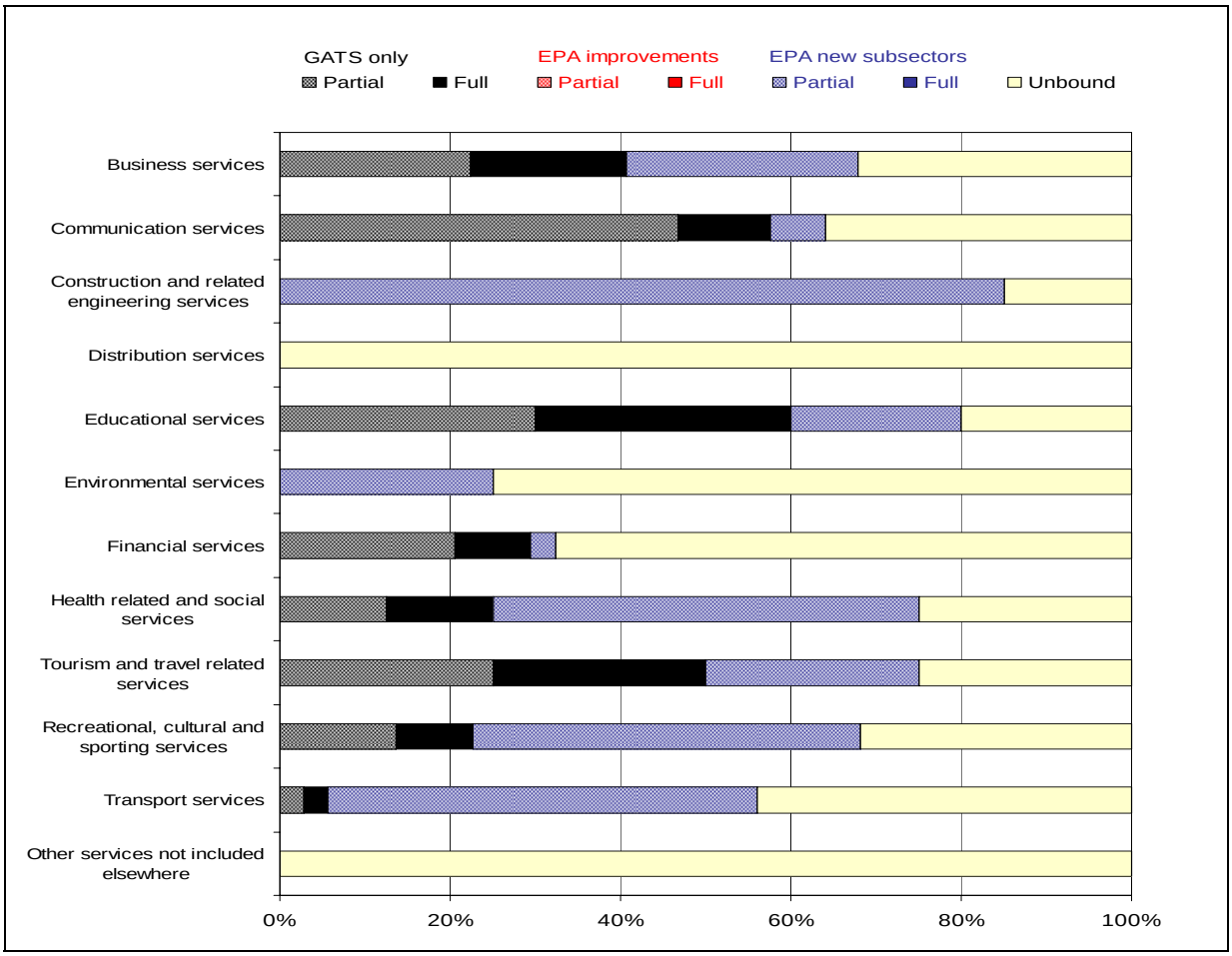
Source: Sauvé and Ward (2009)

Chart 2. Comparing GATS and the EU-CARIFORUMCommitments: Dominican Republic



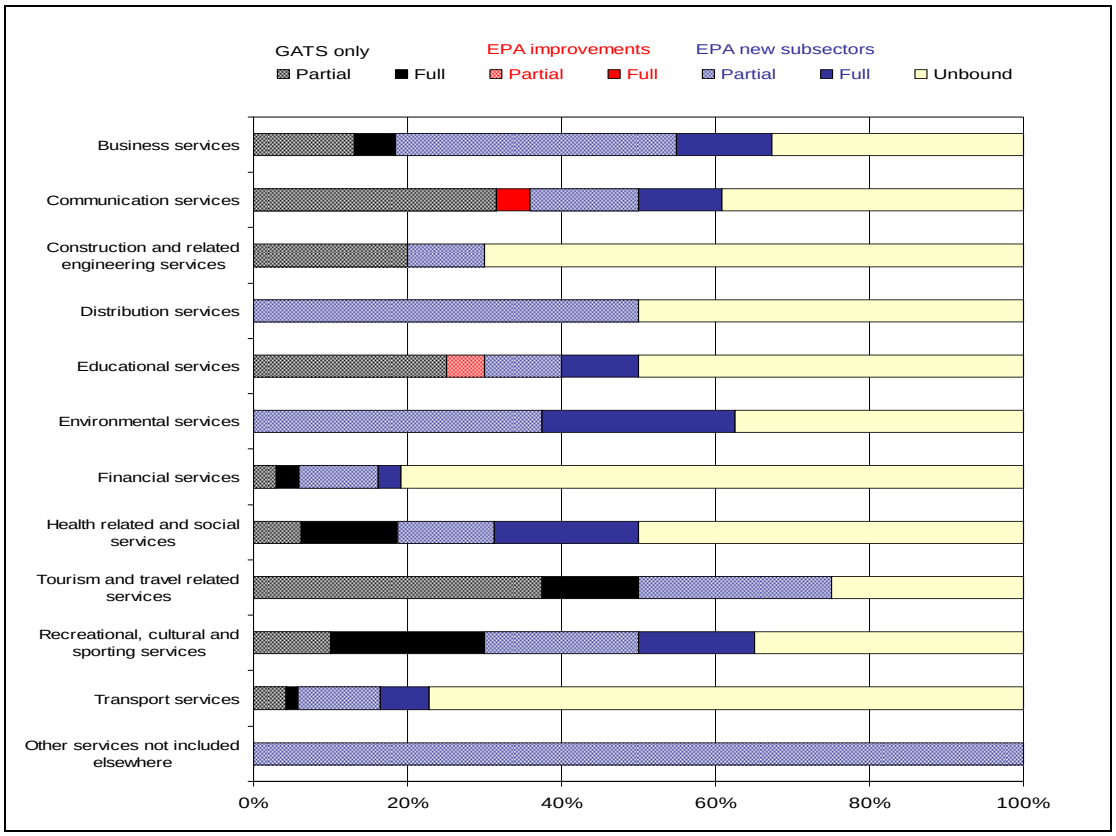
Source: Sauvé and Ward (2009)

Chart 3. Comparing GATS and the EU-CARIFORUM Commitments: Jamaica



Source: Sauvé and Ward (2009)

Chart 4. Comparing GATS and the EU-CARIFORUMCommitments: Trinidad and Tobago



Source: Sauvé and Ward (2009)